REPORT OF WORKING GROUP
ON
STATE FINANCIAL CORPORATIONS

RESERVE BANK OF INDIA

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CHAPTER I

INTRODUCTORY

1.1. A Working Group on State Financial Corporations was set up by the Reserve Bank of India in June, 1962, with these terms of reference, namely,

(1) to review the working of the State Financial Corporations in the light of the policies and procedures followed by them and to evaluate their role in the financing of industries;
(2) to examine the organisational, legal, financial and other difficulties or factors impeding progress of the Corporations, with particular reference to their lending to small industries and to suggest appropriate remedies; and
(3) to suggest ways and means of improving the usefulness of the Corporations generally with a view to facilitating accelerated development of industries.

The following members were nominated by the Reserve Bank of India to serve on this Group:—

1. Shri K. C. Mittra ~~(Chairman)~~
Chief Officer, Industrial Finance Department,
Reserve Bank of India.
2. Shri Bharat Bhushan,
Managing Director,
Uttar Pradesh Financial Corporation.
3. Shri B. K. Chatterjee,
Managing Director,
Madhya Pradesh Financial Corporation.
4. Shri R. S. Pochkhanawala,
Managing Director,
Maharashtra State Financial Corporation.
5. Shri P. C. Malhotra,
Special Officer,
Medium Term Loans Section, State Bank of India.
6. Shri J. S. Raj,
Deputy General Manager,
Industrial Credit & Investment Corporation of India Ltd.
7. Shri C. A. Subrahmanyam,
Secretary,
Industrial Finance Corporation of India.
8. Shri N. M. Chokshi,
Managing Director,
Bank of Baroda Ltd.
9. Shri K. N. R. Ramanujam,
Director, Banking Division,

Economic Department,
Reserve Bank of India.

10. Dr. A. K. Banerji (Member-Secretary),
Deputy Chief Officer,
Industrial Finance Department,
Reserve Bank of India.

After Shri Pochkhanawala left Maharashtra State Financial Corporation, in his place the Bank nominated Shri S. R. Varma, Managing Director, Punjab Financial Corporation. After Shri K. N. R. Ramanujam left India for an overseas assignment, the Bank nominated in his place Shri U. S. Navani who was again succeeded by Shri M. Narasimham, who attended the third and fourth meetings of the Group. The State Bank of India subsequently nominated Shri B. K. Chatterji in place of Shri Malhotra on his retirement. Shri Chatterji attended the third and fourth meetings.

I.2. State Financial Corporations constitute a unique set of institutions established in the different States of India under a Central legislation, the State Financial Corporations Act, 1951. They bear close resemblance to some development banks set up in foreign countries, but there are also significant differences, mainly related to the milieu in which these Corporations function. They have been set up to foster industrialisation, especially in the sector of medium and small-sized industrial units, along the general lines of planned economic development which the country has chosen since 1947.

I.3. Prior to Independence in 1947, the Indian economy, like many other underdeveloped economies of Asia and Africa, was almost stagnant, developing at a rate barely exceeding the growth of population. The economy was characterised by a high ratio of population to natural resources and, in particular, to land. Under the declared industrial policy (in the Industrial Policy Resolution of 1948 and subsequently) and Five Year Plans, the Government of India have been pursuing a deliberate policy of long term economic development, a crucial determinant of which is the pace of industrialisation.

I.4. The First Five Year Plan, speaking of the backward nature of economic institutions in India, expressed that—

> "The problem was not merely one of making the existing economic institutions work more efficiently or making small adjustments in them. What was required was a transformation of that system so as to ensure greater efficiency as well as equality and justice. There were risks in going too far or too fast in these matters, but the risks of not moving fast enough were no less serious."

Again this document has stated that—

> "It is clear that in the transformation of the economy that is called for, the State will have to play a crucial role . . ." in the matter of "satisfying the legitimate expectations of the people."

I.5. During the First and Second Five Year Plans, largely due to the efforts of Government, there was heavy investment in the infrastructure (i.e. power supply, transport, etc.) of the economy. Total investment, public and private, increased from over Rs. 500 crores per annum at the beginning of the First Plan to Rs. 850 crores at its end, and reached an annual level of about Rs. 1600 crores at the end of the Second Plan. As a result, in the decade covered by these two Plans (1951-52 to 1960-61) the economy developed at the average rate of over 4% per annum—the increase in aggregate national income at 1948-49 prices being about 47%; according to preliminary estimates, in 1961-62 the increase in national income was 2.1%*. Foundations were then laid for heavy and basic industries, the previous pattern of industrial production was greatly diversified—which the rate of growth of industrial production cannot fully reflect, and the growth of small industrial units was promoted by special measures. Industrial production showed an average annual rate of increase of 9.1% during 1951-61. In 1962, it gained a further 8.8% over 1961. Neither the rate of growth of national income nor of industrial production can fully reflect the growth-potential of the economy which has been achieved, particularly during the Second Plan period. Although numerous gaps still remain, these developments in the industrial field constitute the foundation on which a complex industrial super-structure will ultimately rest.

I.6. During the Second Plan period, the overall gross fixed investment on the industrial projects of the private sector has been estimated at about Rs. 850 crores, and that of the public sector at Rs. 770 crores, the total gross investment on the programmes of industrial development being Rs. 1620 crores. The Third Plan envisages a considerable step up—gross fixed investment in the private industrial sector is estimated at Rs. 1335 crores, and in the public sector, Rs. 1808 crores, aggregating Rs. 3143 crores. The net investment in the private sector, excluding investment by way of modernisation and replacement, was Rs. 700 crores in the Second Plan period. This is estimated to go up to Rs. 1035 crores in the Third Plan period.

I.7. For public sector industrial projects, except in a few cases, internal resources played a small part in financing new investment in the Second Plan period as these were mostly entirely new ventures, largely financed by advances from Government. The investment programme in the private industrial sector was assisted in some cases by direct Government investment in equity capital or by loans, as in the case of the Rs. 20 crores interest-free loan for steel expansion programme. Otherwise, funds for investment by private enterprise in other fields were largely obtained from two major sources—self financing and foreign capital, including deferred payment arrangements. New issues too yielded

* It is now estimated that the increase during 1951-61 was 43.8%, and during 1961-62 and 1962-63 (preliminary) national income increased by further 2.6% and 2.4% respectively.

about 18% of the resources. These were supplemented by long term loans from specialised institutions set up in recent years, such as the Industrial Finance Corporation of India, State Financial Corporations and the Industrial Credit and Investment Corporation of India Ltd., and from term loans extended by banks. The quantum of funds drawn by private enterprise from each of the recognised sources during the Second Plan and expectations during the Third Plan are estimated as follows:

Source	Estimate for the Second Plan	Expectations for the Third Plan
	(Rs. crores)	(Rs. crores)
1. Institutional agencies	80	130
2. Direct loans from Government	20	20
3. Foreign capital including suppliers' credit	200	300
4. New issues	150	200
5. Internal and other sources	400	600
Total	850	1250

I.8. The estimates of Rs. 80 crores and Rs. 130 crores for the Second and Third Plans respectively from institutional agencies include the contributions of (*a*) the Industrial Finance Corporation of India, (*b*) State Financial Corporations, (*c*) the Industrial Credit and Investment Corporation of India Ltd., (*d*) Refinance Corporation for Industry Ltd., etc. During the first two years of the Third Plan, 1961-62 and 1962-63, financial assistance extended by (*a*), (*b*) and (*c*) may be estimated at about Rs. 57 crores. (The estimates of investment resources expected to be raised from institutional agencies exclude formal term loans from commercial banks for expansion, modernisation, etc.)

I.9. Even though assistance provided by State Financial Corporations appears to be gaining momentum in the last year or two, the joint performance of fourteen Corporations so far, including also within their jurisdiction the three major industrialised States of the country—Maharashtra, Punjab and West Bengal—has been much below expectations. This was responsible for the idea of setting up a Working Group to study in detail the functions of these institutions. It was first suggested by Shri B. Venkatappiah, then Deputy Governor of the Reserve Bank of India, at the Eighth Annual Conference of State Financial Corporations in November, 1961. He had stated at this Conference that it was necessary to consider if, for these Corporations to contribute significantly to economic development, only slight changes in the statute or in their

policies and procedures would suffice or more radical changes were called for. The Chairman of this Conference, Shri H. V. R. Iengar, then Governor of the Reserve Bank of India, was of the opinion that some fundamental changes in the policies and procedures might be necessary to make them function effectively. This is briefly the genesis of the Working Group.

I.10. The first meeting of the Working Group was held in Bombay on the 7th June, 1962, when the draft questionnaire proposed to be issued to State Financial Corporations was broadly approved. Subsequently, another questionnaire was drawn up for being answered by certain other institutions, chambers of commerce and a few prominent individuals. A detailed questionnaire was also framed for eliciting information from certain foreign development banks, the selection of which, from among the very large number of such banks functioning in different countries, was done in consultation with Mr. William Diamond of International Finance Corporation. The three questionnaires are reproduced at the end of this Report. The Group met next on the 20th February, 1963, at Calcutta, and considered the replies received from the various Corporations and such of the institutions, chambers of commerce and individuals which had sent their replies by that date. At the third meeting of the Group at Bombay on 14th October, 1963, members considered the draft report prepared by the secretariat. It was then decided that, after incorporating certain suggestions which members made at this meeting, the revised draft would be placed before the Tenth Annual Conference of State Financial Corporations to be held at Bangalore in January, 1964, for an *informal* discussion on the various recommendations proposed by the Working Group. In December, 1963, the Chairman, another member of the Group and the Member-Secretary held discussions with the State Governments of Andhra Pradesh, Bihar, Maharashtra and Uttar Pradesh and National Small Industries Corporation on some of the issues dealt with in this Report, especially in Chapter II: 'Genesis and present structure of term lending institutions'. The Conference at Bangalore generally endorsed the recommendations of the Working Group, except on certain secondary issues. The fourth meeting of the Group was held at Bombay on Thursday, 6th February, 1964 when the Report was revised having regard to the views expressed at the Conference and signed by the members.

I.11. The scheme of the Report may be indicated briefly. In the next Chapter, the genesis of State Financial Corporations has been indicated; mention has also been made of the other institutions which have been sponsored by Government in the last decade to facilitate the flow of term finance to industry. The problem of co-ordination among these institutions is examined, with particular reference to the functioning of State Financial Corporations. This is followed by Chapters III-VI in which the working of State Financial Corporations since their inception has been reviewed, under certain broad heads—resources, loans and

advances, other permitted business of these Financial Corporations, management and staff, working results and fiscal concessions. This review will generally focus attention on the problems and achievements of State Financial Corporations as a whole, except where some State Financial Corporation merits a special mention; therefore it may, at certain places, not convey the position in particular States. This difficulty is inherent in a brief general survey of a group of institutions which have been set up at different times and have functioned in often very different environments. This review takes into consideration the problems which have been faced so far in these various fields, and the solutions that have been tried, and the recommendations of the Group have been given at appropriate places. The summary of recommendations, in Chapter VII, concludes the Report.

1.12. Throughout this Report, a number of institutions like the Industrial Finance Corporation of India, the Industrial Credit and Investment Corporation of India Ltd., etc. have been often mentioned. It will be convenient to refer to them by their initials rather than their full names, as follows—the Industrial Credit and Investment Corporation of India Ltd.—ICICI, the Industrial Finance Corporation of India—IFC, National Industrial Development Corporation Ltd.—NIDC, National Small Industries Corporation Ltd.—NSIC, the Life Insurance Corporation of India—LIC, Refinance Corporation for Industry Ltd.—RCI, the State Bank of India—SBI, State Financial Corporations set up under the State Financial Corporations Act, 1951—SFCs, and Madras Industrial Investment Corporation Ltd.—MIIC. The word "Corporations" will be used to refer, jointly, to SFCs and MIIC.

1.13. We wish to take this opportunity to thank all State Financial Corporations, the Industrial Finance Corporation of India and Industrial Credit and Investment Corporation of India Ltd., some individuals and chambers of commerce in India and some development banks abroad which assisted us by replying to our questionnaires. Our thanks are also due to State and Central Governments and National Small Industries Corporation Ltd. for the co-operation extended to the Group and for the excellent arrangements made by certain State Governments during the tour undertaken by some of the members of the Group. We are also grateful to the Reserve Bank of India for the facilities placed at the disposal of our secretariat which enabled it to draw freely upon the information and specialised knowledge on these matters available with its Industrial Finance Department throughout our investigations. We particularly wish to record our high appreciation of the hard work put in by the Member-Secretary, Dr. A. K. Banerji, in processing the data collected from various sources and in drafting the Report. We also express our thanks to the secretarial staff who worked very hard to enable the Group to complete its arduous task.

Chapter II

GENESIS AND PRESENT STRUCTURE OF TERM LENDING INSTITUTIONS

Recommendations of the Indian Central Banking Enquiry Committee and the UK Committee on Finance and Trade

II.1. The Managing Agency system was largely responsible for pioneering such limited measure of industrialisation as was achieved in India till the beginning of the last War. The 'twenties and the 'thirties were, however, a period of acute stagnation of the Indian economy, for various reasons. The inflow of foreign venture capital had dwindled considerably, and industrialisation was proceeding at a slower pace as compared with the decades before 1914, and was largely limited to sectors receiving protection from imports by special measures. Except for brief interludes, the stock exchanges were mostly inactive. It is also worth noting that it was largely in this period that Indian enterprise—as distinct from Indian capital—made its debut on the industrial scene, and entered the struggle for a place therein. Perhaps such a situation was an appropriate one for the Indian Central Banking Enquiry Committee, which reported in 1931, to recommend the formation of separate Industrial Corporations in each province. How far this was an echo of similar advice by the Committee on Finance and Trade (Macmillan Committee) in the UK which reported simultaneously with the Indian Committee, or it arose out of the malaise in the Indian capital market, cannot now be determined.

II.2. The Macmillan Committee visualised the functions of the institution which would act as intermediary between industry and investor as follows—acting as financial adviser to existing industrial companies; advising, in particular, as to the provision of permanent capital, its amounts and types; securing the underwriting of and issuing a company's securities to the public and, if necessary, assisting in arrangements in the provision of temporary finance in introduction of an issue; assisting for financing long contracts at home and abroad, or new developments of an existing company, or founding companies for entirely new enterprises, etc.

II.3. The Committee realised that to discharge these functions is often difficult, entailing risks, and involving, in certain cases, temporary locking up of large sums. Hence, such a concern must (*a*) have sufficient capital, with powers to supplement resources by issuing its short term notes; (*b*) be able to rely on the co-operation of existing institutions with large resources to make temporary advances: otherwise it might either fail to carry out its functions or its capital might have to be too big to earn reasonable returns; and (*c*) build up a competent and expert

staff; gradually establish connections in industry; and instil confidence in its issuing ability and credit. The Committee also noted that smaller and medium-sized businesses often found it difficult to raise capital needed by them from time to time, even on perfectly sound security. To provide an adequate machinery to raise long-dated capital in amounts not large enough for a public issue is often difficult. The Committee did not think that this sector of British industry could be served by the larger sized intermediary described above. So an alternative was suggested, viz., to form a company to devote itself to these small industrial and commercial issues only. In addition to its capital, such a company might issue preference shares or debentures.

II.4. The Indian Central Banking Enquiry Committee did not go into such details. After reviewing the facilities available in the capital market, and the working of the State Aid to Industries Acts then in operation in a few provinces, it recommended that Provincial Industrial Corporations be set up. An All-India Industrial Corporation to meet the needs of industries falling within the scope of the Central Government was not ruled out. With regard to Provincial Corporations, the Committee gave its views on their share capital, and its augmentation by debentures, deposits, etc. Contrary to the present scheme of the SFCs Act, 1951, it did not recommend Government guarantee to repay the share capital of the Corporations or to pay dividends on such capital. For debentures, it recommended limited guarantee of interest by Provincial Governments either to the first issue of debentures, or for a certain period of the currency of the debenture issue.

II.5. The few years between 1931 and 1939, during most of which the Great Depression wrought considerable damage to both industrial and agrarian economies, were hardly opportune for such Corporations being set up either in India or in the UK. The Second World War changed the industrial scene of most countries almost overnight, and large sectors of industry were geared to meeting defence needs. Existing units began to be operated on multiple shifts, and their capacity was enlarged. Many new units also came into existence, in both old and new lines of production. Funds for such developments came largely out of the incomes which inflationary financing of defence expenditure brought into being, often supplemented by direct assistance by the Government in setting up units in key industries. Peace-time conditions had, therefore, to be restored before the problems of industrial finance could be viewed again as part of the normal functioning of an economic system.

War and immediate post-war problems of industrial reconstruction in Europe

II.6. The provision of medium and long term finance to industry presented various types of problems in different countries after the last War. In Europe, peace and reconstruction brought enormous demands

for capital. The restoration of war damages, re-equipment of industries overworked or shut down during the war and the need for production to keep pace with the demand for goods and services drove up the demand for industrial capital to levels beyond the capacity of existing institutional arrangements. The mere size of public and private requirements of capital was beyond the limits of what private and institutional investors were able or willing to invest; some of these requirements were also then commercially unattractive. Hence, new institutions and new organisations had to be evolved in many European countries in the critical years of reconstruction and rehabilitation.

II.7. Elsewhere, post-war years saw many industrial finance corporations coming up even in industrially underdeveloped areas which also lacked many of the other appurtenances of a capital market for channelling funds to industry. These corporations, which do not basically constitute a novel device in the capital markets, have now acquired a generic name—development banks—although the similarity of formal title conceals often substantial variations in form and functioning in the different countries. All such institutions have been either sponsored, or in a variety of ways assisted, by Governments, which exert varying degrees of influence over their policies and operations. Apart from a few institutions devoted exclusively or chiefly to the creation or financing of state enterprises, the rest are primarily aimed at stimulating the private sector of the economy of their countries—to act as catalysts for investment in this sector, to provide injections of capital, enterprise and management, and not as administrative devices to handle the Government's own investments. Their functions are closely akin to those of the investment banking institutions of developed countries, though they are intended to be pump primers rather than simply conduits for the factors of production, and they usually have to perform a greater variety of functions.

IFC and the beginning of the idea of SFCs

II.8. In India, the absence of financial machinery specially designed to provide term credit to industry and help in the floatation of shares and debentures—with a view to quickening the pace of industrialisation, led the Government of India to set up the IFC under a separate Act in 1948. Its dealings were statutorily restricted to public limited companies and co-operative societies. Even before this, the Government of Madras had mooted the proposal for a provincial institution to purvey industrial finance in the State, drawing inspiration from two similar companies set up in the UK. After a series of discussions in which the Reserve Bank of India took prominent part, Madras Industrial Investment Corporation Ltd. was set up in March, 1949. Earlier, in 1946, the Bank was also consulted on the proposal of the Government of Punjab for setting up a corporation for this State under the Companies Act. In January, 1949, the Government of Bombay decided to set up an Industrial Credit Corporation to supplement the work of IFC by making finance available

to medium and small scale industrial units. The Punjab Government urged the Centre that since the functions of the proposed corporation would be distinct from those of a company registered under the Companies Act, it was desirable to govern it by a separate statute.

II.9. We may here recapitulate briefly the background of the proposed legislation for State corporations. After introducing the IFC Bill in the Central Legislature, the Finance Minister had moved that the Bill be referred to a Select Committee. Speaking on this motion, he recognised the need for other corporations, and disclosed his intention that after the IFC Bill was passed, he would persuade the Provinces to set up similar corporations mainly to finance small scale industrial units. Earlier he had cited examples from other countries of the co-existence of two complementary institutions, for financing large scale and small and medium scale units. In this connection, he referred also to the recommendations of the Indian Central Banking Enquiry Committee to which a reference has been made earlier.

II.10. To complete the background for the SFCs Act, 1951, we may add that, in addressing a circular letter to State Governments on the proposed legislation in September, 1949, the Central Government stated as follows:

> "The Bombay Government wish to set up a provincial Industrial Credit Corporation for making financial aid available to medium and small scale industries to supplement the work of the Industrial Finance Corporation established by the Government of India. They consider that, as in the case of the Central Corporation, the provincial Corporation should be established under a special statute in order to make it possible to incorporate the required provisions in regard to majority control by Government, guarantee by Government, restriction of distribution of profits, special powers of recovery of dues, etc. Since under entry 33 in List I in the Seventh Schedule read with Section 100 of the Government of India Act, 1935, the incorporation, regulation and winding up of trading corporations including financial corporations, fall within the purview of the Central Legislature, they have requested the Government of India to enact the necessary legislation. The proposal has been discussed by the Government of India with the Bombay Government, the Reserve Bank of India and the Industrial Finance Corporation. There is a general agreement that there is scope for provincial Industrial Credit Corporations . . ."

Elaborating the need to set up State Corporations, Government also pointed out that, for various reasons, the arrangements under which States gave loans to private industries under the different State Aid to Industries Acts were extremely inadequate.

II.11. After considering the views of the Provincial Governments on the above circular letter embodying the proposal for a Central legislation to set up Corporations at the State level, in April, 1950, Government circulated a draft bill for comments, particularly as to whether its provisions met all necessary requirements. After obtaining the views of

the concerned parties as also of Reserve Bank, the SFCs Bill was introduced in Parliament in December, 1950. The Act came into force on 1st August, 1952.

The Setting up of SFCs

II.12. Although the SFCs Act came into force on the 1st August, 1952, the first SFC was registered under this Act in Punjab in February, 1953. Of the fourteen SFCs now functioning in different States, one was set up in 1952-53—Punjab, three in 1953-54—Bombay, Kerala and West Bengal, four in 1954-55—Assam, Bihar, Rajasthan and Uttar Pradesh, and three in 1955-56—Andhra Pradesh, Madhya Pradesh and Orissa, by which time almost all States were covered, except Mysore and Jammu & Kashmir which had their SFCs in 1958-59 and 1959-60. The present Gujarat SFC, set up in May, 1960, is a result of the bifurcation of the previous Bombay SFC. As already stated, the State of Madras has been served since March, 1949 by MIIC, a company registered under the Companies Act but later brought under the purview of the SFCs Act only with regard to Sections 37A and 38 relating to inspection by, and submission of periodical returns to, the Reserve Bank of India. Of the Centrally administered areas, the jurisdiction of Punjab Corporation was extended to cover Delhi in October, 1957, and Himachal Pradesh in July, 1962; that of Assam Corporation was extended to cover Tripura in March, 1960, and a Tripartite Agreement among the Assam Government, Tripura Administration and Manipur Administration for extention of the jurisdiction of Assam Corporation to Manipur was executed on the 1st April, 1963. Nagaland, NEFA, Goa, Daman and Diu, Pondicherry, Laccadive, Amindivi & Minicoy Islands, and Andaman & Nicobar Islands are not yet served by any Corporation.

Special features of the statute of SFCs as a variant of development banks

II.13. As mentioned earlier, there are now scores of term financing institutions in different countries coming under the general description of development banks. Some are statutory bodies, others joint stock companies, and some function as wings of their Governments. A number of them have developed close connections with international financial agencies and markets, including the International Bank for Reconstruction and Development. SFCs, however, seem to form a rather unique set of institutions. A very considerable range of their functions is influenced both by the State Governments under the statute which governs these institutions and by the environment of an under-developed economy, with its own socio-economic features inhibiting the emergence of a modern industrial sector. To these are added the special problems which are constantly arising when a low-income, largely agrarian, economy strains all its resources for industrialisation under democratic planning. Thus, as their name suggests, these institutions are State sponsored

statutory bodies; the funds of the State Governments as well as of the Reserve Bank of India are employed in these corporations; the States have guaranteed minimum dividends on the share capital of these corporations as well as all borrowings by them either as deposits or as bonds and debentures; perhaps because of the financial involvement of the States in these institutions, the statute has given SFCs special powers of recovery of their loans which are more than those available to any corporate body registered under the Companies Act; the States have a say in the management of these corporations through nomination of directors, issue of directions to auditors of SFCs for special audit, issue of instructions in the light of Reserve Bank's inspection reports, and on questions of policy; their dealings are limited to industrial concerns as defined statutorily, which exclude housing, trading, certain service industries, plantations, etc.; there is also statutory restriction as regards the maximum size of assistance to individual units which has been fixed at Rs. 20 lakhs for public limited companies or co-operatives and Rs. 10 lakhs for other types of concerns; also there is constant exhortation by Government that they may devote increasing attention to financing small units, irrespective of the economics of lending such small amounts as far as these corporations are concerned; security requirements for loans have been laid down statutorily in general terms which have tended to be interpreted rather strictly; no SFC can be liquidated except by the order of the State Government and in such manner as it may direct.

Major amendments to SFCs Act

II.14. Since the enactment of the SFCs Act in October, 1951, there have been two major sets of amendments, in 1956 and 1962; there was one important amendment in 1955 also, viz., addition of the words "to be engaged" in the definition of an "industrial concern" under section 2(c). This empowered SFCs to have dealings with concerns newly set-up but not yet engaged in manufacture, preservation and processing of goods, etc. The major amendments are shown below, grouped under eight different heads, including a few miscellaneous amendments. These amendments, which have generally had the effect of widening the powers and functioning of SFCs, will be taken up again in the body of the Report at relevant places. Attention has been drawn to them at this stage as they are significant for an assessment of the functioning of these Corporations over the last decade. (Figure in brackets at the end of each item indicates the year in which the Act was amended.)

1. Section 2(c): *Definition of industrial concern*

Includes concerns "to be engaged" in the manufacture, etc. of goods . . . . (1955). Also includes concerns engaged/to be engaged in hotel industry, in the transport of passengers or goods by road or by water or in the development of any contiguous area of land as an industrial estate (1962).

2. Section 7: *Borrowings (including bonds and debentures) by* ■ *SFC*

(*i*) Borrow money from Reserve Bank, repayable on demand or on the expiry of fixed periods not exceeding 90 days against securities of the Central Government or any State Government (1956).

(*ii*) Among the securities for borrowings mentioned at (*i*) have been included other trustee securities (excluding immovable property) and bills of exchange and promissory notes eligible for purchase or rediscount by Reserve Bank or fully guaranteed by a State Government (1962).

(*iii*) Borrow from (*a*) Reserve Bank upto 60% of its paid-up capital for a fixed period not exceeding 18 months against securities of the Central Government or of any State Government of any maturity or against its bonds and debentures guaranteed by the State Government and maturing within a period not exceeding 18 months; (*b*) the State Government in consultation with Reserve Bank; and (*c*) with prior approval of Reserve Bank, from any financial institution notified by the Central Government (1962).

(*iv*) The limit of outstanding bonds and debentures and the contingent liabilities in the form of guarantees or underwriting agreements, together with borrowings mentioned at (*iii*) was raised from 5 to 10 times SFCs' paid-up share capital and reserve fund (1962).

3. Section 8: *Deposits*

(*i*) Accept deposits from State Government and with the prior approval of the State Government and Reserve Bank from local authorities also (1962).

(*ii*) Minimum period for which deposits can be accepted reduced from 5 years to one year (1962).

(*iii*) All deposits (except those from the State Government itself) shall be guaranteed by the State Government (1962).

4. Section 25(1): *Business which SFC may transact*

(*i*) Act as agent for the Central Government or the State Government or Industrial Finance Corporation in the transaction of any business with an industrial concern in respect of loans or advances granted or debentures subscribed by them (1956) and also for any other financial institution notified by the Central Government (1962).

(*ii*) Transact the following business: (*a*) guaranteeing loans raised by industrial concerns from scheduled banks and State co-operative banks; and (*b*) guaranteeing deferred payments due from any industrial concern in connection with its purchase of capital goods within India (1962).

(*iii*) Shares, etc. taken up in fulfilment of underwriting obligations may be retained beyond 7 years only with the prior permission of Reserve Bank (1962).

(*iv*) Subscribe to 'right' shares, offered by the concern whose shares are taken up by it in fulfilment of underwriting obligations. (The 'right' shares cannot be retained after the original shares have been disposed of) (1962).

(*v*) Permitted (*a*) to convert debentures subscribed or loans granted into stock or shares of the concern in cases where an option is attached to such debentures/loans for being so converted and (*b*) to subscribe to 'right' issues offered by the concern whose shares have been taken up in conversion as at (*a*) above (1962).

(*vi*) Subject to the overall limit referred to at 2(*iv*) above, the aggregate of contingent liabilities on account of guaranteeing of loans and deferred payments and underwriting must not exceed twice SFC's paid-up capital and reserve fund; this limit may be exceeded upto thrice the paid-up capital and reserve fund with the prior approval of the State Government and in consultation with Reserve Bank (1962).

5. Section 25(2): *Security*

Grant loan/subscribe to debentures/guarantee loans without any security provided guarantee of State Government or scheduled bank or State co-operative bank is available (1956).

6. Section 26: *Limit of accommodation*

The limit of accommodation (guaranteeing/granting of loan or subscription to debentures) to an industrial concern was raised from Rs. 10 lakhs to Rs. 20 lakhs in case of public limited companies and co-operative societies, the limit for private limited companies and other types of concerns, etc. remaining unchanged at Rs. 10 lakhs. The stipulation that the accommodation should not exceed 10% of the paid-up share capital of SFC was removed in respect of accommodation to all types of industrial concerns (1962).

7. Section 35A: *Special Reserve Fund*

Constitute a special reserve fund to which shall be transferred such portion of the dividends payable to the State Government and Reserve Bank on their shareholdings, as may be fixed by mutual agreement. However, the total amount in this fund shall not exceed 10% of the paid-up share capital of SFC (1962).

8. Miscellaneous

(*i*) *Section 3A :* Provision was made for having joint financial corporations for two or more States (1956).

(*ii*) *Section 10(f) :* The State Government is required to consult Reserve Bank while appointing Managing Director (1962).

(*iii*) *Section 29 :* In case of default by industrial concern in respect of repayments of loans and advances or of failure to comply with the terms of its agreement with the Corporation, right of transfer by lease was granted (1956).

(*iv*) *Section 37A :* Reserve Bank can inspect the working of SFC and its books and accounts on direction from Central Government (1956).

(*v*) *Section 39 :* The State Government is required to consult Reserve Bank before issuing instructions on questions of policy to SFCs (1956).

(*vi*) *Section 46A :* Provision for extending the jurisdiction of an existing Corporation to other territories in consultation with Reserve Bank (1956).

Other term lending institutions in India and their co-ordination with SFCs

II.15. Apart from IFC and SFCs, a few other agencies too were set up in the 'fifties under Government auspices for the supply of term

funds to existing and new industrial units. As the development of the economy in the First Plan period was unfolding itself, it was evident that, unlike the First Plan, the Second Plan would have to make much larger provisions to lay the foundations of industrial development. The free working of the market mechanism could not be expected to ensure that resources would in fact be directed—in the right quantity and at the right time—to the selected industrial sectors. Institutional arrangements had thus to be devised to serve such an end. This would provide the needed incentives and thereby influence the deployment of scarce resources in the desired directions.

II.16. The other term lending agencies which Government have sponsored are, in chronological order, National Industrial Development Corporation Ltd. (1954), National Small Industries Corporation Ltd. (1955), the Industrial Credit and Investment Corporation of India Ltd. (1955), Refinance Corporation for Industry Ltd. (1958) and the various State Small Industries Corporations (since 1958) and State Industrial Development Corporations (since 1960). These are aimed at filling the gaps in the structure of financial institutions for the supply of term funds to industry in the private sector in particular (NIDC sponsors units in the public sector as well).

II.17. The Life Insurance Corporation of India (LIC) is also an important source of long term investment finance for industry. In recent years, the underwriting activity of LIC, ICICI, IFC and leading banks has been an important factor in the new issues market. Government have also set up a few wholly State-owned corporations as limited companies, viz., Film Finance Corporation of India Ltd. and Rehabilitation Industries Corporation Ltd. to assist the film industry and for rehabilitating persons displaced as a result of the Partition of India respectively. While there is much in common as regards the objectives of these various corporations, there are also important differences in regard to capital structure, ownership of shares, extent of Government control, methods and field of operation, etc. The existence of these different corporations has also raised questions of co-ordination of their policies.

II.18. As already stated, IFC was the first financial corporation to be set up in India, in 1948. It is jointly owned by the Central Government, the Reserve Bank of India and financial institutions. Broadly, the object of IFC is to make medium and long term credit available to public limited companies and industrial co-operatives, particularly in circumstances where normal banking accommodation is inappropriate or recourse to capital issues impracticable. There are no maximum limits upto which it can sanction loans to individual concerns but under the IFC Act loans over Rs. 1 crore require prior approval of Central Government.

II.19. National Industrial Development Corporation Ltd. (NIDC) is a fully Government-owned limited company. It was set up in 1954 for the promotion and development of industries for securing a

balanced and integrated growth of the industrial structure, both in the public and private sectors. It is not a financial institution in the strict sense of the term as, in addition to financing modernisation, etc. in existing industrial units which have an important place in the economy, it directly formulates and implements industrial projects of importance. Its impact is, perhaps, more of a qualitative nature, in changing the industrial structure of the country by filling up important gaps; the magnitude of its financial assistance may not therefore appear impressive. It is primarily a development corporation and its function as a financing agency is confined to providing rehabilitation and modernisation finance to selected industries, viz., cotton and jute textile, and machine tool industries. Its working funds come from Government as grants and loans.

II.20. National Small Industries Corporation Ltd. (NSIC) was established by the Central Government in 1955, pursuant to a recommendation of the International Planning Team of the Ford Foundation, as a fully Government-owned concern, specifically to assist the growth of small scale, industries through promotional, marketing, financing (mainly supply of machines on hire-purchase) and other activities. For its resources, it depends entirely on Government which have furnished share capital, substantial loans, and grants for the promotional activities. Its major achievement has been the procurement and distribution of machines, both indigenous and foreign, to small enterprises on hire-purchase terms.

II.21. The establishment of the Industrial Credit and Investment Corporation of India Ltd. (ICICI) in 1955 was a landmark in the field of industrial financing from institutional sources. It differs from IFC and SFCs in ownership, management, and operations. It is a public limited company registered under the Companies Act and was set up with the support of the Government of India, International Bank for Reconstruction and Development, Commonwealth Development Finance Company, and foreign and Indian banking and insurance interests. As a joint stock company (not having been set up under a special statute) its operations are characterised by greater flexibility. Its object is the development, expansion, and modernisation of private sector industries by providing long term finance in the shape of loans and equity participation, by underwriting issues of capital, etc. It has been assisted by Government by a large interest-free loan repayable in 30 years, and another interest-bearing loan for a shorter period. Government are also guaranteeing the substantial foreign borowings it is contracting. With its foreign exchange resources, it has been able to support many new units in the chemical and other fields where plant, etc. needed to be imported. Unlike IFC and SFCs, from its inception ICICI has played an active role in providing risk capital by its underwriting operations and direct subscriptions to shares of industrial concerns.

II.22. Refinance Corporation for Industry Ltd. (RCI) was estab-

lished in 1958 as a joint stock company with the support of Reserve Bank, SBI, LIC and major commercial banks. The question of expanding the role of the commercial banking sector in providing term finance to industry, to a limited extent, and providing these banks with suitable inducements was being considered by Government for a long time. In 1954, the Committee on Finance for the Private Sector (Shroff Committee) had advocated longer term borrowing facilities for banks from Reserve Bank for this purpose. The offer of assistance, amounting to Rs. 26 crores, from the US counterpart funds—PL 480—provided a suitable occasion to set up RCI, and achieve through it the reorientation of the banking system in the direction of term lending.

II.23. State Small Industries Corporations (SSICs) and State Industrial Development Corporations (SIDCs) are the latest additions to the institutional set-up. They are the counterparts, at the State level, of NSIC and NIDC respectively, which function as all-India institutions. As far as SSICs are concerned, the Second Five Year Plan had envisaged that industrial estates to be set up by State Governments should be run through special Corporations or such other agencies as the Governments may decide. Subsequently, at the 14th meeting of the Small Scale Industries Board, the Chairman—Shri Manubhai Shah, stated that a small industries corporation in each State was proposed to be set up for taking over complete management of industrial estates and for providing the necessary facilities such as opening of raw material depots, marketing services, and hire-purchase of indigenous machinery. This recommendation was endorsed by the Working Group constituted by the Board to draw up the programme of work for the Third Plan, and later communicated by the Government of India to State Governments for implementation.

II.24. With the exception of Jammu & Kashmir, Madras and Nagaland, SSICs have been established so far in all the other States. SIDCs have been set up so far only in seven States viz. Andhra Pradesh, Bihar, Gujarat, Kerala, Maharashtra, Orissa and Uttar Pradesh. Like the all-India institutions, almost all these State Corporations are fully Government-owned limited companies except (*a*) SSICs in Gujarat and Orissa which are public limited companies, where the State Governments have power to nominate certain number of directors on their Boards and (*b*) Maharashtra and Gujarat SIDCs which are statutory bodies.

II.25. Although according to the Working Group referred to above and the decision of the Small Scale Industries Board, the functions of SSICs were restricted to the setting up and management of industrial estates, organising supply and marketing services, running of common service facility centres, etc. leaving the provision of finance to the appropriate financial institutions like SFCs, SBI and other commercial banks, while setting up SSICs, the State Governments have framed their functions to include lending as well. Broadly, the functions of the existing SSICs are to counsel, finance, protect and promote the interests of

small scale industrial units and to provide them with capital, credit and technical and managerial assistance. They can also promote and operate specific schemes to develop small units. All the Corporations (with the exception of those in Orissa and Gujarat) can grant and guarantee loans to small units and invest their funds in or deal with shares, etc. of any company. In practice, they have confined themselves to one or more of the following activities, viz., setting up and managing industrial estates, organising depots for supply of raw materials, running of common service facility centres and sales emporia, supply of indigenous machinery on hire-purchase basis to small units and providing assistance to small units to participate in the stores purchase programme of the State Governments. The financial assistance granted by these Corporations so far is negligible, except in one or two States.

II.26. The functions of SIDCs are generally to assist and finance the promotion, establishment and execution of medium and large-sized industrial undertakings and projects. The scope of their activities has been kept wide deliberately, to enable them to accelerate the pace of industrial development in the States by directly promoting and executing various projects as well as by indirectly helping others to do so. However, most of them are still in the formative stages. The older ones, viz., in Andhra Pradesh, Kerala and Uttar Pradesh, which have been in existence for about two years, have undertaken financial activities to some extent e.g., underwriting and direct subscription to shares. Andhra Pradesh Corporation has also sanctioned an outright loan of Rs. 10 lakhs repayable in 5 years to an applicant company. The contribution of these Corporations in other fields has, however, been negligible.

II.27. In July, 1960, the Government of India introduced the Credit Guarantee Scheme for small industries to enlarge institutional finance, particularly from commercial banks, to small units by sharing the risks inherent in loans and advances to such units. The objective of the scheme is to induce selected commercial and co-operative banks, and SFCs (including MIIC) to increase their loans and advances to small units. Since the beginning of 1963, the scheme has been extended to the whole of India from a few selected districts where it was introduced in 1960 as an experimental measure.

II.28. The setting up of RCI and the introduction of the Credit Guarantee Scheme are primarily—although SFCs and State co-operative banks are covered by them—intended to induce, by reimbursement and guarantee facilities, the banking system to play a more direct role in providing term loans to industry and larger finance to small scale units.

II.29. There is now, thus, a network of special institutions for providing term finance to industry in the private sector. [The Appendix to this Chapter indicates a summary position of the sources of funds and financial assistance granted to industry by some of these special institutions as at the end of December, 1962 (ICICI) or March, 1963 (SFCs,

etc.) or June, 1963 (IFC & MIIC)]. These institutions, whether Government-owned or privately owned, statutory bodies or limited companies, have been set up on the initiative of, and with financial support from, Government and Reserve Bank. It must now be ensured that their activities are duly co-ordinated, avoiding overlapping of operations, and jointly providing loans and underwriting facilities wherever necessary. As the spheres of operations of IFC and SFCs are gradually being extended to underwriting, and of IFC to direct subscriptions to shares, there is need for co-ordination and co-operation between them and ICICI.

II.30. It may be held by some that co-ordination among these agencies, that is, establishing proper relationships among them, is a function of time which will mould each of them to the shape necessary for survival. But survival itself may not always denote the utility of an institution in the wider context. Also, to have deliberately set up these agencies under State sponsorship is itself an evidence of our decision that market forces and the play of natural selection are not to have the upper hand in determining the course of developments. Having thus set up these agencies, it must be examined if the necessary and sufficient conditions for their effective functioning have been assured and if they are in the proper mutual relationship in which no institution overshadows the growth of another, and each has its specific field to serve. It is necessary to do this early enough so that the needed changes may be introduced before the inconsistencies, if any, get hardened. This Working Group is concerned with SFCs only, and so we limit ourselves to pointing to a few major aspects vis-a-vis SFCs where rethinking seems necessary.

II.31. One of the basic aims in setting up SFCs was to make institutional finance available to small units and to channellise through them most of such funds as States normally disbursed to small units departmentally. But having enacted the statute for SFCs in 1951, and after some States had taken the initiative in the matter, the Central Government set up NSIC late in 1955, pursuant to a recommendation of the International Planning Team of the Ford Foundation which toured this country in 1953. The primary purpose for which the Corporation was set up was to provide the necessary incentive and help to small industrial units to improve their techniques of production and management gradually by working on assured orders from Governmental buying agencies. As broadly envisaged by the Planning Team, namely that the proposed Corporation should "contain a separate financial body, with power to direct loans to small industry for improving their equipment", it was also entrusted with the scheme of supply of machinery on hire-purchase basis, in addition to a number of promotional activities. Shortly afterwards NSIC also obtained necessary foreign exchange to import machines from abroad. The Five Year Plans had greatly increased the demand for machinery of all types from small, medium and large enter-

prises, many of which were prepared to back up their demand by the offer of prices considerably higher than the listed prices, on account of import restrictions. The entry of NSIC in the field at this juncture, with the added facility of being able to supply imported machinery at normal and not inflated prices, and on hire-purchase, was certainly of great value to small and ancillary units. Besides, NSIC's procedures were more simple than those of SFCs and, under its hire-purchase scheme, the purchasers had to find resources for a smaller margin than for mortgage loans. This must have affected the business of SFCs with small units which would have otherwise obtained finance from the Corporations for acquiring machines.

II.32. From the inception of the Hire-Purchase Scheme in 1956 upto 30th September, 1962, NSIC had accepted 9003 applications involving 37,961 machines valued at about Rs. 37 crores. A breakdown of these applications by range of values presents a significant picture:

	Range of value of applications	%
i.	Upto Rs. 25,000	64
ii.	From Rs. 25,001 to Rs. 50,000	16
iii.	From Rs. 50,001 to Rs. 1 lakh	11
iv.	From Rs. 1 lakh to Rs. 2.5 lakhs	6
v.	Above Rs. 2.5 lakhs	3
		100

II.33. While at the interest rates now charged by SFCs, it may not pay them to handle smaller applications—group (*i*) in particular, i.e. applications upto Rs. 25,000, the rest could certainly go to them if it is an accepted policy that autonomous, decentralized institutions, functioning at the State level, should cater to the needs of small units.

II.34. Even on the score of the cost at which NSIC supplies hire-purchase finance, the scales seem tilted in favour of SFCs for applications of over Rs. 50,000. In such cases, except where applicants are industrial co-operatives, NSIC charges interest at 6% p.a., the repayment being generally spread over 7 years. It also levies a service charge at 6% on the c.i.f. or f.o.r. value of machines, imported or indigenous respectively. For an application for machines valued at Rs. 1 lakh, and where repayment is spread over 5 years, the financing charges to the purchaser work out to over 8%. The present concessions to co-operatives, ancillaries, etc. are now proposed to be withdrawn with a view to making NSIC a viable unit.

II.35. It is for serious consideration if, in the fitness of things, NSIC may not concentrate all its energies and resources on promotional activities which hold great promise, including helping the procurement of machines—both indigenous and imported—for such commission as

may be mutually agreed upon, and give up its hire-purchase business which SFCs should take up. That is, all small borrowers wanting machines on hire-purchase basis would only approach SFCs for their requirements; NSIC, as a promotional body, would act as the clearing house for information regarding availability, price and performance, etc. of different types of machines, and also as an agent of SFCs for the procurement of machines wherever borrowers want such services. With regard to applications involving small amounts, which are considered as uneconomic for SFCs to handle except on better terms, Government may give them a direct subsidy on a suitable formula, rather than the concealed subsidy which NSIC is now getting in the shape of equity capital from Government, etc. In the alternative, such applications may be handled by SSICs.

II.36. Before SFCs can take up this business, however, the Act will have to be suitably amended. Also initially SFCs cannot undertake hire-purchase of machines imported by NSIC against specific foreign credits as necessary arrangements will need to be entered into with the foreign lenders to bring SFCs into the scheme. It is suggested, therefore, that after the Act is amended, in one or two selected States where SFCs have acquired considerable experience in lending to small units, all applications for hire-purchase may be dealt with by SFCs with the assistance of Small Industries Service Institutes, where necessary, and with NSIC acting as the clearing house for information, as suggested earlier. It would be desirable to associate a few senior officers of NSIC with the management of these SFCs in this transitional phase. The experience gained in these pilot States would be of use in extending the scheme to other States.

II.37. Of the four types of financing institutions, IFC, SFCs, ICICI and NSIC, SFCs alone are denied foreign exchange resources. It was thought that SFCs would develop participation arrangements with the other agencies for foreign exchange loans. But this has not been possible. It may be held that units which need exchange for importing machines and approach SFCs for funds for such imports as also for other block assets may approach Government for an exchange allotment if the industries concerned are of value to the economy. But small and medium units which form the bulk of the clientele of SFCs often experience considerable difficulty in getting such exchange in competition with large, influential units. In the case of small units particularly, NSIC, by virtue of having foreign exchange at its disposal, must be taking over a good part of business from SFCs. If SFCs are to develop and finance the newer types of industries which have a marked growth potential, are vital for meeting defence needs, and help to raise the technological level of our industrial structure, it will be desirable to make arrangements to meet at least a part of their foreign exchange needs. Some foreign loans which Government may get for them may carry interest such as would leave them a smaller margin of profit than on their rupee loans. But

the exchange component may easily be lent at a higher rate of interest as certain development banks abroad also do.

II.38. On the implementation of the above suggestion, ICICI and IFC may informally undertake that normally they would not entertain applications for financing import of machines below an agreed figure so as to avoid duplication of facilities which SFCs could provide. As SFCs cannot at present offer foreign exchange loans, ICICI, for example, is entertaining applications for relatively medium-sized loans which should really lie in the field of SFCs.

II.39. As indicated earlier, SSICs and SIDCs recently established in the States have been authorised to cover a wide field of activities, closely overlapping some of the functions of SFCs. If this policy has arisen out of dissatisfaction with the slow growth of business of SFCs, or because of certain restrictive provisions in the SFCs Act, the remedy could have been to inject more dynamism into the working of SFCs by various means and remove the restrictive provisions wherever necessary and desirable. Or the States might have felt the need for a fully State-owned and controlled institution to take up development projects. Here again it must be stressed that SFCs are as efficient as the new institutions to translate industrial projects, especially after the amendment of 1955 which enables them to finance concerns yet "to be engaged" in production, etc. This Working Group is of the view that further proliferation of institutions with like functions and jurisdictions may be avoided. Technical personnel for running such institutions are in short supply and maximum use should be made of them in existing institutions. However, since a number of these new corporations are already in existence, there is need for preventing duplication of their functions with those of SFCs and bringing about co-ordination of their activities, wherever possible. This may largely be ensured by restricting the functions of these institutions to those which do not encroach upon the functions of SFCs. Thus, SSICs may be restricted to the provision of marketing facilities for the products of small industries, organising depots for supply of raw materials to them, etc. As far as the supply of machinery on hire-purchase basis is concerned, it is recommended that SFCs should take this up, except in the case of applications for very small amounts which may be dealt with by SSICs. Normally, these institutions should not grant direct loans and advances to industrial concerns and, thereby, impinge upon the main function of SFCs.

II.40. Regarding SIDCs, it is suggested that the scope of their operations may be restricted to the performance of functions of a purely promotional nature e.g., formulating, executing and running of projects which are necessary to fill gaps in the industrial structure of the States. As stated earlier, some SIDCs have entered the field of underwriting of issues of capital, direct investment, etc. and this has to some extent restricted the directions in which SFCs could have extended their operations gradually. If these corporations restrict their promotional

activities to the assuming of risks which SFCs would not normally be prepared to undertake under their present set-up, there is not likely to be much conflict of functions at least till such time as SFCs enter these fields which they, as development banks, must do ultimately. But as in the case of SSICs, SIDCs also should not extend the scope of their operations to the sphere of direct loans and advances to industrial units, at least within the statutory limits permitted to SFCs. It is also suggested that funds proposed to be advanced by State Governments to industrial concerns on a commercial basis may be routed through SFCs.

APPENDIX TO CHAPTER II

Summary position of sources of funds and financial assistance granted by development banks to industry

(Rs. mn.)

Name of Development Bank	Position as on	Paid-up Capital			Reserves and Surplus	Bonds and Debentures	Borrowings			Other Liabilities	Total Liabilities/ Assets	Financial Assistance			
		Govt.	Foreign Sources	Total			From Govt.	Foreign Currency	Total			Outstanding loans and advances	Subscriptions to shares, debentures, etc.: In pursuance of underwriting agreements	Subscriptions to shares, debentures, etc.: Total	Amount disbursed
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)
Industrial Finance Corporation of India	June 30, 1963	14.0	—	70.0	30.0	282.4	247.5	21.8	269.3	168.5	820.2	597.6	32.5	50.7	1025.7(a)
State Financial Corporations	March 31, 1963	64.8	—	140.0	3.7	161.4	—	—	12.1	44.9	362.1	250.5	0.5	2.7	330.5
Madras Industrial Investment Corporation Ltd.	June 30, 1963	10.2	—	13.2	1.2	23.6	—	—	12.1	103.6(b)	153.7	69.4	32.1	42.7	97.8
National Industrial Development Corporation Ltd.	March 31, 1963	4.5	—	4.5	—	—	97.4	—	97.4	2.7	104.6	97.5	—	3.5(c)	125.6
Industrial Credit & Investment Corporation of India Ltd.	December 31, 1962	—	15.0	50.0	15.8	—	145.0	100.8	245.8	7.2	318.8	166.4	50.8(d)	75.9(e)	282.6(a)
National Small Industries Corporation Ltd.	March 31, 1963	5.0	—	5.0	12.9		54.2	11.3	65.5	27.3	110.7	70.2	—	—	112.8(f)
Refinance Corporation for Industry Ltd.	March 31, 1963	—	1.5(g)	25.0	0.4(h)	—	145.0	—	145.0	4.2	174.6	161.3	—	—	177.9
Total		98.5	16.5	307.7	64.0	467.4	689.1	133.9	847.2	358.4	2044.7	1412.9	115.9	175.5	2152.9

(a) Includes subscription to shares, etc. and guarantees. (b) Includes Rs. 80.4 million as deposits and cash certificates. (c) Investment in shares of fully-owned subsidiary company. (d) Cumulative disbursement. (e) Includes investments of the Corporation in industrial securities. (f) Value of machines delivered. (g) Held by foreign banks. (h) Does not include balance of Profit & Loss Account to be appropriated.

Chapter III

RESOURCES OF SFCs—THEIR SOURCES OF SUPPLY AND COST

Introductory

III.1. The resources of a development bank like a SFC broadly consist of (*i*) share capital, (*ii*) deposits, (*iii*) borrowings, and (*iv*) reserves. Development banking itself being largely a post-war phenomenon, especially in the relatively underdeveloped countries, there is as yet no set or accepted pattern in which these constituents of resources must arrange themselves for optimum results, except some fairly broad and flexible, conceptual, ratios relating owned and borrowed funds, etc. Also, the parties contributing to constituent items (*i*) to (*iii*) are seen to vary considerably from one country to another. Thus, the role of the State has been far from uniform in the different countries. In the case of many development banks abroad, and of ICICI in India, considerable amounts of both equity and loan funds have come from extra-national sources, like foreign banks and investment companies, International Bank for Reconstruction and Development, International Development Association, Marshall Plan funds, etc. Further, not all development banks are statutory bodies. Actually, only a minority are so. This factor too has contributed to a measure of diversity in their capital structure and business methods and policies. SFCs are statutory bodies and as such are subject to considerably detailed statutory provisions governing their policies and operations. The provisions relating to the above four constituents of resources are considered below together with the manner in which these have facilitated the raising of the requisite funds on terms suitable for their operations. It must be stressed even here that these institutions are still, in many ways, in their embryonic stage; they have yet to develop those organic links with the rest of the—often much older—sections of the capital market to ensure a freer flow of resources and expertise between themselves and the latter.

Share Capital

III.2. Under Sec. 4 of the SFCs Act, 1951, the authorised capital of each SFC shall be fixed by the State Government; in no case it shall be less than Rs. 50 lakhs or exceed Rs. 5 crores, divided into as many fully paid-up shares as the State Government may determine, which will also, with the approval of the Central Government, determine the number of shares to be distributed among these categories of shareholders—(*a*) the State Government, (*b*) Reserve Bank, (*c*) scheduled banks, insurance companies, investment trusts, co-operative bank or other

financial institutions, and (*d*) others (including individuals). Not more than 25% of the shares may be allocated to category (*d*).

III.3. Under Sec. 6 of the Act, these shares are guaranteed by the State Governments as to the repayment of principal and payment of annual dividend at such minimum rates as the Governments may fix with the approval of the Central Government. This is an almost unique feature of development banks in India. It is almost unknown in foreign countries where such development banks have been set up, often under even more difficult circumstances than in India. The only foreign bank with such a stipulation seems to be the Industrial Development Bank of Turkey for which the Government guaranteed a dividend of 6% only during the first three years of the bank's establishment. The liability was actually met only in the first year, after which the bank paid dividends out of profits. The purpose in India was, presumably, to attract funds from investors. But it will be seen below that, for some reason or other, this expectation has been only partly fulfilled. The guaranteed rate of dividend is 3% p.a. for Punjab SFC, earliest to be set up under the Act, and 4% for Jammu & Kashmir and Mysore SFCs which were set up in 1959. In the case of Orissa SFC, the rate was 3½% upto April, 1962, increased to 4% for the fresh capital of Rs. 50 lakhs raised in May, 1962. For all the other ten SFCs, it is 3½%. In terms of Sec. 35(2), the sum that any State Government may pay under this guarantee is repayable. Under Sec. 6(2), the shares of SFCs are deemed to be on par with securities enumerated in Sec. 20 of the Indian Trusts Act, 1882, and are also approved securities for purposes of the Insurance Act, 1938, and the Banking Companies Act, 1949. The shares of MIIC are entitled to a dividend of 3% p.a., guaranteed by the State Government.

III.4. As on 31st March, 1963, the authorised capital of the various SFCs ranged from Rs. 50 lakhs in Jammu & Kashmir to Rs. 4 crores in Andhra Pradesh. The authorised capital of Maharashtra SFC was fixed at Rs. 1 crore in 1962 in terms of the Scheme of Reconstitution of Bombay SFC which had an authorised capital of Rs. 4 crores. It was Rs. 3 crores in Uttar Pradesh and Rs. 2 crores for the rest ten SFCs. On the same date, the paid-up capital was the lowest in Jammu & Kashmir, viz., Rs. 50 lakhs. It was Rs. 1.5 crores in Andhra Pradesh and Rs. 1 crore in the remaining SFCs. On 31st March, 1963, the paid-up capital of MIIC was Rs. 1.32 crores.

III.5. Paid-up capital is initially determined by the State Government (in consultation with Reserve Bank) having regard, inter alia, to the stage of industrial development of the region, the immediate and future needs for finance from industry and other considerations. In an industrially less developed State like Orissa, the paid-up capital was originally Rs. 50 lakhs in March, 1956. It was raised to Rs. 1 crore in May, 1962. Similarly, the paid-up capital of Gujarat SFC was fixed at Rs. 50 lakhs at inception in May, 1960, and increased to Rs. 1 crore

in September, 1961. As in the case of authorised capital, the paid-up capital of Maharashtra SFC was fixed at Rs. 1 crore in place of Rs. 2 crores for Bombay SFC by conversion of shares of Rs. 1 crore of the latter into bonds.

III.6. The distribution of shareholdings of all SFCs together as in March, 1963 is given below:

Class of shareholder	Value of share-holding (Rs. lakhs)	% to total
1. State Government	647.7	46.3
2. Reserve Bank of India	244.3	17.5
3. Scheduled banks, insurance companies, etc.	455.8	32.5
4. Others	52.2	3.7
Total	1400.0	100.0

State Governments are the largest single class of shareholders. Together with Reserve Bank, they held 63.8% of the shares. The intention, it may be recalled, is that the State Government and Reserve Bank should together hold a majority of the shares in any one SFC to ensure a controlling interest. In Orissa and Kerala, their holding was as high as 84% and 76% respectively. In Assam, it was 72% and in Uttar Pradesh, 70%. Only in West Bengal and Rajasthan, the holdings of institutions like scheduled banks, insurance companies, etc. were high at 45% and 38% respectively.

III.7. Thus, despite the State Governments' guarantee of dividend and principal, the response from banks, insurance companies, etc. in taking up shares of SFCs has been generally below expectations. This may be largely because the guaranteed dividend is not considered sufficiently attractive. But the lack of ready marketability of the shares, which is discussed later, and even the fact that SFCs are statutory bodies in the management of which the State Government would have a large say, might also have kept away prospective investors. But a higher rate of dividend would certainly attract more capital from private sources and reduce the dependence of these institutions on the State. If these institutions are to seriously develop their business, particularly underwriting and gradually also equity financing, then such Corporations which undertake these businesses on a sufficiently large scale would need to have a stronger capital base to absorb the shocks of likely losses than would be necessary for a purely lending institution.

III.8. Table I shows the percentage distribution of shares among the various classes of holders. Scheduled banks have contributed most

TABLE I

Percentage distribution of shares of State Financial Corporations among the various classes of shareholders as on 31st March, 1963

Corporation of	Classes of Shareholders					
	State Government	Reserve Bank	Scheduled banks	Co-operative banks	Insurance companies, investment trusts and other financial institutions	Others
(1)	(2)	(3)	(4)	(5)	(6)	(7)
1. Andhra Pradesh	46.7	13.3	15.3	3.7	15.0	6.0
2. Assam	51.7	20.0	14.2	2.0	9.5	2.6
3. Bihar	40.0	15.0	12.7	14.7	7.6	10.0
4. Gujarat	36.0	20.0	27.2	2.4	10.4	4.0
5. Jammu & Kashmir	57.6	20.0	12.5	0.1	7.4	2.4
6. Kerala	60.4	15.3	2.5	0.2	19.6	2.0
7. Madhya Pradesh	58.4	15.0	18.0	0.3	2.2	6.1
8. Maharashtra	32.8	18.1	24.9	2.3	19.0	2.9
9. Mysore	40.5	15.0	25.3	2.1	16.6	0.5
10. Orissa	64.2	20.0	6.3	1.3	8.1	0.1
11. Punjab	41.7	20.0	19.2	5.0	10.8	3.3
12. Rajasthan	36.2	21.0	27.0	—	11.3	4.5
13. Uttar Pradesh	55.4	15.0	16.0	1.2	9.9	2.5
14. West Bengal	31.8	20.0	22.2	2.7	20.1	3.2

in Maharashtra, Gujarat, Rajasthan and Mysore, followed by West Bengal, Punjab and Madhya Pradesh—perhaps more a reflection of the efforts of the sponsors than of the relative resources of banks in these States. Co-operatives, as would perhaps be expected, have contributed only small amounts, except in Bihar (15%) which again is somewhat surprising as the movement in this State is generally considered much weaker than in, say, Punjab, Maharashtra or Andhra Pradesh. Insurance companies, including LIC, investment trusts and other financial institutions have contributed 15-20 per cent in Andhra Pradesh, Kerala, Maharashtra, Mysore and West Bengal. These data further reiterate the need to attract subscribers other than the State Government and Reserve Bank.

Acceptance of deposits by State Financial Corporations

III.9. In terms of Sec. 8 of the SFCs Act, as amended in April, 1962, a SFC may accept from the State Government or, with prior approval of the State Government and Reserve Bank, a local authority or any other person, deposits repayable after the expiry of a period which shall not be less than 12 months; the total of such deposits shall not at any time exceed the paid-up share capital of the SFC. All such deposits, other than the deposits of the State Government, shall be fully guaranteed by the State Government as to the repayment of principal and payment of interest. Prior to the amendment of April, 1962, the minimum period for which deposits could be accepted was five years and there was no provision for Government guarantee.

III.10. Until recently, only two SFCs, viz., Kerala and Andhra Pradesh had been accepting deposits from the public. The response was not encouraging. In Andhra Pradesh, the State Government has extended its guarantee upto a limit of only Rs. 25 lakhs. Deposits accepted by these two SFCs and outstanding as on 31st March, 1963, were:—(*a*) Andhra Pradesh State Financial Corporation (@ 4¾% for periods of 5 years)—Rs. 1,10,980 and (*b*) Kerala Financial Corporation (@ 4% to 4½% for periods of 5 years)—Rs. 3,55,500, or a total of Rs. 4,66,480. Under the amended provisions, so far Kerala and Maharashtra SFCs have obtained the permission of Reserve Bank and the guarantee of the respective State Governments for accepting deposits, the latter upto Rs. 1 crore. Other SFCs as well as State Governments may expedite the preliminaries before deposits can be accepted. States may extend guarantee for deposits upto the ceiling permitted in the Act, viz., paid-up capital, straightaway. A piecemeal approach is both time-consuming and not conducive to fostering public confidence in these institutions.

Terms and Conditions

III.11. Prior consultation with Reserve Bank regarding the terms and conditions for deposits is necessary to ensure that the interest

rates offered are not out of tune with the prevailing market conditions, and that deposits carrying State Government guarantee are not attracted at uneconomic rates. The rates proposed to be offered by Maharashtra and Kerala SFCs have been approved by Reserve Bank, and are the same as larger commercial banks (having deposits of over Rs. 50 crores) offer under the Inter-bank Agreement on Deposit Rates, namely—

For 12 months & over but less than 24 months	4 % per annum
For 24 months & over but less than 48 months	4¼% ,,
For 48 months & over but less than 60 months	4½% ,,
For 60 months & over	5 % ,,

III.12. Under the Inter-bank Agreement on Deposit Rates, medium and small-sized banks (having deposits of above Rs. 25 crores and Rs. 10 crores respectively) are allowed to offer one-eighth of one per cent to one-quarter of one per cent more than these standard rates. Though deposits with SFCs are fully guaranteed, as against the maximum of Rs. 1,500 in respect of individual deposits with commercial banks insured under the Deposit Insurance Scheme, as SFCs cannot provide depositors with the facility of advances against such deposits which banks can, they may, where necessary, offer upto 25 nP. per cent per annum more interest than the medium-sized commercial banks.

III.13. Reserve Bank has also been suggesting to SFCs to lay down a minimum amount for individual deposits and to fix a suitable upper limit for individual deposits for shorter periods of one to two years so that they might be in a position to meet such commitments on due dates without having to stretch their resources. Thus, Maharashtra and Kerala SFCs have fixed Rs. 1,000 and Rs. 10,000 respectively as the minimum limits for individual deposits. For the former, the upper limit of individual deposits has been fixed at Rs. 50,000 for shorter periods of one to two years. Latter has fixed the upper limit for individual deposits at Rs. 5 lakhs and Rs. 10 lakhs for one year and two years respectively. The minimum limit fixed by Kerala SFC may be rather high in comparison with fixed deposits accepted by banks. This may keep away prospective depositors. As it is, banks have an advantage over SFCs. They can offer other services to depositors which SFCs cannot. So it seems that SFCs may fix such minima as would enable them to take full advantage of raising resources in the shape of deposits. Unlike SFCs, MIIC which is not governed by the provisions of the SFCs Act referred to above and which can, therefore, accept deposits in excess of its paid-up capital and for periods below 12 months, has succeeded in attracting deposits of over Rs. 8 crores (as on 31st May, 1963), of which Rs. 6.92 crores were fixed deposits and the rest, call and short term deposits. The rates offered by it compare very favourably with those permitted under the Inter-bank Agreement. Thus, for deposits upto one year, MIIC and the Inter-bank Agreement rates are 4½% and 3¾% respectively; for deposits of 1-2 years, 4¾% and 4% respectively; for 2-3

years, 5% and 4¼% respectively; for 3-4 years, 5¼% and 4¼% respectively; and for over 5 years, 5½% and 5% respectively. In the last three maturity groups, MIIC offers a further 25 nP.% for deposits of Rs. 1 lakh and above. As with SFCs, these deposits are also fully guaranteed by the State Government. It is felt that the rates offered by MIIC are rather high and should be brought into closer relationship with the rates under the Inter-bank Agreement. The Group is in agreement with this view.

III.14. Many SFCs hold that the raising of funds by deposits is more convenient and economical as it avoids the considerable overhead expenses associated with bond issues. The acceptance of deposits has also a certain advantage over the raising of funds in bulk by issuing bonds. Former ensures a steady flow of funds; the rates of interest could be varied with the situation in the money market and to accommodate particular customers or types of customers as is not unusual with banks. Also, as deposits are repayable on different dates, the SFC does not have to find funds for redemption in one lot as in the case of bonds. Finally, this method avoids some part of the loss that might be incurred by SFCs in placing funds raised by way of bonds in deposit with banks which fetch lower interest than is payable on bonds. With adequate publicity, canvassing and local patronage, they may be able to attract reasonable amounts of deposits, including those of Trust Funds (which are not available to banks). Local bodies like Municipalities, etc. may also be encouraged to keep their surplus funds on deposit with the Corporations. SFCs may also consider if they may not all join together to undertake an intensive all-India campaign to advertise, and focus attention on, the various facilities that they offer to the public—both for deposits, which are fully guaranteed by the State Governments and for their financing, and guaranteeing, etc. functions for prospective borrowers for industrial purposes.

III.15. SFCs stand at a certain disadvantage in attracting deposits as, not being banks, they cannot give advances against their deposit receipts. To remove this difficulty, it is suggested that deposit receipts isued by SFCs may be made assignable to third parties. Depositors needing advances could then assign these receipts to banks. Such an assignment may be possible if the terms and conditions governing deposits made with SFCs, inter alia, recognise that depositors will be entitled to assign the deposit balances covered by the deposit receipts to third parties. SFCs could also lay down an appropriate form of a letter by which depositors can transfer the balances represented by the deposit receipts; as also the form of a notice (conforming to the requirements of Sec. 131 of the Transfer of Property Act) to be given by the depositors to SFCs. To encourage the public to keep deposits with SFCs, assignment of deposit receipts may be exempted from stamp duty. It is suggested that State Governments may take necessary action in this behalf.

III.16. The total loans granted by SFCs and outstanding as at the end of March, 1963 (which was the end of the second year of the Third Plan), aggregated Rs. 25.31 crores, representing a net increase of Rs. 6.66 crores over the level as at the end of March, 1962. Considering the increased industrial tempo that would be generated during this Plan, reinforced now by defence activity, the annual requirement of funds by SFCs may soon easily go up to Rs. 15 to 20 crores. To help meet such a high demand on the resources of SFCs, it may be desirable to permit them to receive deposits upto twice rather than only one time the paid-up capital. The more energetic SFCs can then profit from this source of funds.

III.17. The effort to attract deposits from the public may appear somewhat unorthodox. Few foreign development banks give much attention to this source, which may account for the present statutory limit on deposits of SFCs. But the amendment of 1962, which introduced State guarantee of deposits and reduced their minimum period to one year, seems to suggest that the legislature had come round to accord a larger measure of importance to deposits than it was perhaps prepared to in 1951. In India, the raising by SFCs of at least a part of their resources through deposits may be emphasised for, inter alia, the following reasons: (*a*) with the full guarantee of such deposits as against only a partial guarantee for deposits in commercial banks, it should be possible to collect sizable funds and canalise them into productive employment; (*b*) such deposit resources would be a second line of defence for SFCs as bonds are not always easy to float; and (*c*) the present interest structure on deposits of different maturities compares favourably with the interest and other costs of floating bonds. In the section on bonds below, the somewhat controversial question of financing medium term lending with resources obtained for shorter periods is discussed and it has been shown that the present and near prospective period-wise pattern of lending by SFCs is such that some part of it can be judiciously financed by deposit-resources, particularly when account is taken of the standby borrowing arrangement from Reserve Bank for 18 month periods, incorporated in the SFCs Act in 1962.

Borrowings, including issues of Bonds

III.18. Sec. 7 of the Act provides that a SFC may raise funds (*i*) by issuing bonds and debentures and (*ii*) by borrowing from Reserve Bank, the State Government, and any financial institution notified by Central Government. As regards (*i*), Sec. 7(1) provides that a SFC may, in consultation with Reserve Bank, issue and sell interest-bearing bonds and debentures which shall be guaranteed by the State Government concerned as to the repayment of principal and the payment of interest. The rate of interest is to be fixed by the State Government on the recommendation of the Board of the SFC and with the approval of the Central Government.

III.19. As regards (*ii*), in terms of Sec. 7(2) borrowings against prescribed securities from Reserve Bank are repayable (*a*) on demand or on the expiry of a fixed period not exceeding 90 days from the date on which the money is borrowed and (*b*) on the expiry of a fixed period not exceeding 18 months. While there is no limit in the Act for borrowings under (*a*), those under (*b*) shall not exceed 60% of the paid-up capital of the SFC. A SFC can also borrow (*a*) from the State Government, in consultation with Reserve Bank, on such terms as may be agreed upon, and (*b*) with the prior approval of Reserve Bank, from a financial institution notified in this behalf by the Central Government. (RCI alone has been so notified.)

III.20. Under Sec. 7(5), the total amount of bonds and debentures issued, borrowings (other than those from Reserve Bank repayable on demand or on the expiry of fixed periods not exceeding 90 days) and contingent liabilities of the SFC in the form of guarantees given or underwriting agreements entered into by it, shall not exceed ten times the paid-up share capital and reserve fund of the SFC. A similar limit is there for IFC as well. But in the case of Agricultural Refinance Corporation, total borrowings from the Central Government (including the interest-free loan), Reserve Bank and other approved institutions, together with the outstanding amount of bonds and debentures and deposits shall not exceed 20 times its paid-up capital and reserve fund. For SFCs, the multiple of 10 times the paid-up capital may be relaxed, especially as it covers contingent liabilities as well. Since under Sec. 7(5), all borrowings from the State Government, notified financial institutions, and from Reserve Bank (for 18 months) are also included in this multiple, perhaps the easier way to relax would be to make the multiple 15 instead of 10, than to exclude some of these borrowings from the multiple. Since for all such borrowings SFCs have to consult/obtain the prior approval of Reserve Bank, there is no scope for apprehension that a SFC may suddenly be found to have borrowed too heavily. Some development banks abroad have no restrictions on their borrowings while certain others e.g., the Industrial Credit Bank of Japan can borrow above the limit fixed for SFCs, viz., upto 20 times the paid-up capital and reserves. The position regarding bonds issued and other borrowings of SFCs is reviewed below.

Bonds issued: So far, all SFCs except those of Gujarat, Jammu & Kashmir and Orissa have issued bonds. The total amount of bonds issued varies from Rs. 0.5 crore in case of Andhra Pradesh, Rajasthan and Madhya Pradesh SFCs to Rs. 2.5 crores in case of Punjab and Madras Corporations. Some Corporations, viz., those in Assam, Punjab, West Bengal and Madras have approached the market as many as four times. The total outstanding liability of twelve SFCs as on 31st March, 1963, on account of bonds issued by them was Rs. 16.15 crores as shown below:

Corporation of	Bonds outstanding (Rs. lakhs)
1. Andhra Pradesh	54.99
2. Assam	182.00
3. Bihar	150.25
4. Gujarat	39.29(a)
5. Kerala	109.70
6. Madhya Pradesh	55.00
7. Maharashtra	274.22(b)
8. Mysore	130.20
9. Punjab	267.02
10. Rajasthan	50.05
11. Uttar Pradesh	101.83
12. West Bengal	200.00
Total of SFCs	1614.55
13. Madras	236.07
Total of all Corporations	1850.62

(a) Transferred from Bombay SFC consequent on division of assets and liabilities of that SFC between Maharashtra and Gujarat SFCs.
(b) Amount includes Rs. 1 crore issued in 1962-63 by conversion of an equivalent amount of shares, consequent on reconstitution of Bombay SFC.

III.21. The yearwise floatation of bonds reveals the uneven pace of borrowings by these Corporations:

Bond Floatations—yearwise

	(Rs. lakhs)
1956-57	36.14
1957-58	323.79
1958-59	255.08
1959-60	105.00
1960-61	—
1961-62	792.94
1962-63	257.20
Total	1770.15

After raising Rs. 5.79 crores in 1957-58 and 1958-59, there was a lull, and only Rs. 1.05 crores were borrowed in the next two years. The spurt

came in 1961-62 when Rs. 7.93 crores were raised—followed by a lull in 1962-63: Rs. 2.57 crores. But for the emergency and the provision for borrowing from Reserve Bank for 18 months and from RCI, (and also a certain slackening of industrial activity since late 1962), there would again have been a large demand for funds this year since sanctions have grown rapidly in the last two years. Without adequate institutional support for bonds, the Corporations would soon face a serious shortage of resources.

III.22. The following breakdown into amounts subscribed by various institutions, etc. to the bonds issued upto 31st March, 1963 (excluding the issue of Rs. 1 crore by Maharashtra SFC in 1962-63) by all the Corporations (including MIIC) would show that commercial banks other than State Bank (46%) and LIC (26%) have, between them, taken up about 72% of the total amount.

	Amount (Rs. lakhs)	% to total
1. Governments	10.41	0.6
2. Reserve Bank of India	30.21	1.7
3. Life Insurance Corporation of India	467.29	26.4
4. State Bank of India	126.43	7.1
5. Commercial banks	810.20	45.8
6. Co-operative banks	63.01	3.6
7. Insurance companies, investment trusts, other financial institutions	21.32	1.2
8. Other institutions	166.47	9.4
9. Individuals	74.81	4.2
Total	1770.15	100.0

III.23. Table II shows the breakdown (in percentages) of subscriptions by various subscribers to these bonds. The share of Reserve Bank varied from 0.5% in the case of the 1961 issue of Andhra Pradesh, to 15.2% in the case of the 1958 issue of West Bengal. If requested, Reserve Bank generally now takes up these bonds—if needed—upto a maximum of 10% of the public subscription or the shortfall, whichever is less. It has so far subscribed only to 11 bond issues out of a total of 29 issues in respect of which the breakdown among subscribers is available. The States also have participated in only two issues—by Bihar and Madras. The bulk of the subscription to almost all the issues has been from LIC and commercial banks. Subscription by LIC varied from 5.0% in the case of the Bihar issue of 1958 to 63.6% in the case of the Assam issue of 1962. The share of commercial banks varied between 2.1% in the case of the Madras issue of 1956 to 93.3% in the case of its

TABLE II

Percentage contribution for each floatation of bonds by SFCs and MIIC for issues upto 31st March, 1963

Corporation of	Date of issue	Amount Rs. lakhs	State Government	RBI	LIC	SBI	Commercial banks	Co-op. banks	Ins. cos., investment trusts, etc.	Other institutions	Individuals
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
1. Andhra Pradesh	22- 5-1961	54.99	—	0.5	42.2	3.5	39.8	—	—	—	14.0
2. Assam	15-11-1959	55.00	—	—	45.5	13.6	35.8	1.8	0.9	—	2.4
	26- 4-1961	50.00	—	—	50.0	15.0	31.0	4.0	—	—	—
	26- 2-1962	55.00	—	—	63.6	9.1	20.8	4.1	2.4	—	—
	25- 3-1963	22.00	—	—	—	22.7	72.7	4.6	—	—	—
3. Bihar	15- 9-1958	100.25	0.9	1.0	5.0	6.0	52.1	7.0	0.2	23.1	4.7
	24-10-1961	50.00	—	7.5	10.0	5.0	44.0	4.0	—	14.5	15.0
4. Kerala	21- 3-1958	55.00	—	4.4	13.6	9.2	45.4	2.1	8.1	13.2	4.0
	10- 1-1962	55.00	—	—	54.6	—	15.6	0.5	1.8	27.2	0.3
5. Madhya Pradesh	30- 3-1962	55.00	—	—	41.2	7.3	42.7	4.6	4.0	—	0.2
6. Maharashtra	7-11-1957	116.51	—	13.1	—	5.4	47.6	1.7	1.1	8.9	22.2
	12- 1-1962	110.00	—	—	9.1	6.0	21.1	4.6	0.5	41.2	17.5
7. Mysore	8- 1-1962	55.00	—	—	8.5	4.3	87.2	—	—	—	—
	1-11-1962	75.20	—	—	26.6	—	62.5	9.5	—	1.3	0.1

8. Punjab	7- 1-1958	102.28	—	—	9.8	9.8	78.4	1.7	0.1	0.1	0.1
	8- 5-1961	54.90	—	—	45.6	8.3	45.8	—	—	—	0.3
	9- 5-1962	55.00	—	—	54.6	7.7	37.6	—	—	—	0.1
	22-10-1962	55.00	—	—	54.6	8.1	37.3	—	—	—	—
9. Rajasthan	8- 1-1962	50.05	—	—	40.0	10.0	40.0	—	—	10.0	—
10. Uttar Pradesh	13-10-1958	54.83	—	—	15.3	0.3	65.0	15.3	—	0.6	3.5
	29- 1-1962	53.00	—	—	28.3	9.4	53.8	3.8	4.6	0.1	—
11. West Bengal	24- 3-1958	50.00	—	15.2	30.0	15.3	35.2	—	—	4.0	0.3
	1- 3-1960	50.00	—	—	17.2	12.9	14.5	—	7.4	43.5	4.5
	13- 1-1962	50.00	—	—	38.5	8.2	11.6	3.1	—	38.5	0.1
	8-11-1962	50.00	—	—	50.0	10.0	38.5	—	0.5	1.0	—
Total for SFCs (Rs. lakhs)		1534.01	0.88	30.21	419.29	116.43	670.11	47.09	18.11	158.32	73.57
Percentage		100.0	—	2.0	27.3	7.6	43.7	3.1	1.2	10.3	4.8
12. Madras	1- 9-1956 } 9-11-1956 }	36.14	—	—	49.8	—	2.1	43.8	—	1.3	3.0
	1-10-1958	100.00	—	—	—	5.0	93.3	—	1.2	0.3	0.2
	1- 3-1962	100.00	9.5	—	30.0	5.0	46.0	—	2.0	7.4	0.1
Total for all Corporations (Rs. lakhs)		1770.15	10.41	30.21	467.29	126.43	810.20	63.01	21.32	166.47	74.81
Percentage		100.0	0.6	1.7	26.4	7.1	45.8	3.6	1.2	9.4	4.2

1958 issue. As regards State Bank, its subscription varied from 0.3% in the case of the Uttar Pradesh issue of 1958 to 22.7% in the case of the Assam issue of 1963.

III.24. For the relatively small sums for which these institutions have as yet approached investors in recent years, they have thus depended on two major sources. No doubt some have been supported by other miscellaneous sources, as the following data show, but the subscriptions by other groups have been negligible.

Co-operative banks	15.3%	Uttar Pradesh	1958 issue
	43.8%	Madras	1956 ,,
Other institutions	23.1%	Bihar	1958 ,,
	41.2%	Maharashtra	1962 ,,
	27.2%	Kerala	1962 ,,
	43.5%	W. Bengal	1960 ,,
	38.5%	,,	1962 ,,
Individuals	14.0%	Andhra Pradesh	1961 ,,
	15.0%	Bihar	1961 ,,
	22.2%	Maharashtra	1957 ,,
	17.5%	,,	1962 ,,

The need to have a wide clientele for these bonds would seem to be particularly strong when the Corporations would be coming to the market, very soon perhaps, for drawing away annually as much funds as they have done so far cumulatively from their inception. Both LIC and commercial banks may then be led to tighten their fists when other parties would have to be approached. In fact, in 1963, LIC did not contribute any amount to the $4\frac{3}{4}$%-1975 bonds issued by the Assam SFC, which collected only Rs. 22 lakhs against its requirement of Rs. 50 lakhs, nor to the $4\frac{3}{4}$%-1975 bonds of Maharashtra SFC for Rs. 1 crore.

III.25. As at the end of 1961, LIC had total investments of Rs. 581.54 crores (as against Rs. 527.11 crores as at the end of December, 1960). Of this, Rs. 400.23 crores or 69% were in Government and other approved securities and Rs. 102.63 crores were in debentures and preference and ordinary shares of joint stock companies. Of its total investments in 'approved securities' (other than Government securities) of Rs. 46.37 crores, investment in the ordinary shares and bonds of IFC, SFCs and MIIC was Rs. 4 crores or 8.5%, and less than one per cent of total investments. (By March, 1963, however, LIC had contributed Rs. 5.19 crores to the bonds of IFC and Rs. 4.67 crores to the bonds of SFCs and MIIC).

III.26. As SFCs have often run short of funds or found it difficult

to raise funds from the market, it will be very desirable to enter into an arrangement with LIC by which it would be prepared to invest, on demand, upto about 2% to 3% of its total investments in the bonds of these institutions. Latter would thus be provided with more funds and a more flexible access to sources of finance. As these bonds are guaranteed by State Governments, they are also safe for LIC. The implementation of this suggestion that LIC should make available to SFCs lines of credit will enable these institutions to draw funds according to, rather than in anticipation of, their requirements. When a SFC raises resources by bond issue and disburses the funds over a period of 1 to 2 years, in this interim period the undisbursed amounts can only be invested in banks, fetching one to two percent lower returns than what is to be paid to bond holders. The current procedure thus reduces the profitability of operations of SFCs.

III.27. It is reported that LIC has agreed to set apart annually Rs. 6 crores for land mortgage banks' debentures, as perhaps the raising of agricultural produce, which such debentures are expected to further, has been accorded a high priority in our planning. It is also understood that if these banks absorb this amount "fruitfully", every effort would be made to raise the amount further. In the context of putting up the maximum defence effort, industrialisation is no less a priority undertaking, and the proposal made above, therefore, deserves serious consideration. It will also be desirable for State Bank to extend more support to SFC bonds in future. Simultaneously, attempts should be also made to interest other investors, including individuals, in these bonds. We have given later our recommendations to achieve this.

III.28. The rate of interest at which SFCs issue bonds is generally $4\frac{1}{4}\%$—$4\frac{3}{4}\%$, usually 25 nP.% more than the interest rate on loans floated by the Central and State Governments. Some SFCs arrange for underwriting their issues with a commission of generally 38 nP.%, in addition to 12 nP.% generally paid by way of brokerage. The issue prices of the last floatations of bonds of the various Corporations are given below:

	Issue Price	Discount
	(Rs.)	(Rs.)
Andhra Pradesh	100.00%	—
Assam	100.00%	—
Bihar	98.00%	2.00
Kerala	100.00%	—
Madhya Pradesh	100.00%	—
Madras	100.00%	—
Maharashtra (Bombay)	100.00%	—
Mysore	99.75%	0.25
Punjab	99.50%	0.50
Rajasthan	99.50%	0.50
Uttar Pradesh	99.00%	1.00
West Bengal	100.00%	—

The maximum discount allowed was 2% by Bihar SFC. Over the years, discounts on bonds of some of the SFCs e.g., Bombay, Punjab, West Bengal, Assam and Mysore, have been reduced. For instance, in 1959 and 1961, Assam Financial Corporation offered discount of 50 nP.% but the latter issue carried a 25 nP.% higher interest; but in 1962, it raised the rate by a further 25 nP.% to 4.75% before it could issue bonds at par. The first issue by Mysore Corporation in 1962 was offered at a discount of 50 nP.% but on its second issue in the same year, discount was reduced to 25 nP.% only by putting up interest by 25 nP.% which raised yields. Bombay Corporation too offered a discount of 1.50% in respect of its issue of 1957. Its 1962 issue was floated at par. As both issues were at 4½%, the SFC got the latter on more favourable terms.

III.29. Discount is significant for the running and redemption yield of bonds only in association with the rates of interest. These determinants of yield have often not displayed parallel movements in the different Corporations as the market conditions for different floatations were not identical. Some Corporations have been able to attract subscribers despite giving them a lower yield than in their earlier issues. Others —notably MIIC—have had to weigh their baits more heavily, either by the offer of higher interest rates or of larger discounts. Bonds floated during 1961 and 1962 seem to show a trend towards higher yields. In the present state of stock markets, it is doubtful if SFCs can raise sizable funds unless they offer higher returns than in the past, and it will not be economical for them to do so without raising their lending rates too. This aspect has been discussed later in Chapter IV.

III.30. Under the SFCs Act, these bonds are issued in consultation with Reserve Bank, which co-ordinates the issues of various SFCs as well as the loan programmes of the Central and State Governments. In view of the tight condition of the money market in recent years, some SFCs, particularly those away from money market centres e.g., Bihar, had to do considerable canvassing to attract investors. This is due, among other things, to the fact that SFC bonds are permitted to be issued only after the Government borrowing programme is completed and large funds have been drained away from the market. To remedy the situation, it has been suggested in some quarters that the States may include the probable requirements of the Corporations while drawing up their own annual loan programmes, and transfer such funds to them on the same terms on which these are borrowed, with perhaps arrangements for sharing the expenses on a pro-rata basis. The Corporations will no longer have to pay slightly higher rates of interest on their loans than the State Governments. The feasibility of this suggestion may be examined.

III.31. The maturity peiod of SFC bonds is generally 10-12 years. Subscription to these bonds by commercial banks has been declining for almost all SFCs. Apart from the fact that in recent years banks have

reduced their holdings of Government and other trustee securities, mainly to meet the increasing demands for loans and advances, their reduced interest in SFC bonds may be due to their longer maturity periods as compared to some of the recent Central and State Government loans. Thus, in July, 1960, the Central Government floated 3½% Bonds, 1966, with the issue price at Rs. 99.75 per cent and in 1961, 3½% National Plan Bonds (third series), 1967, at Rs. 98.90 per cent and a further tranche of the 3½% Bonds, 1969, at an issue price of Rs. 98.40 per cent. Again in July, 1963, they floated two new loans,—(*i*) a further tranche of existing 4% loan, 1969, at Rs. 99.50 per cent, and (*ii*) 4¼% loan, 1973, at par. Some State loans too were of shorter maturity than SFC bonds. Thus, in 1960-61, twelve States floated loans for a maturity period of 9 years only, at 4% interest.

III.32. No doubt, as against the reduced contribution made by banks, LIC has increased its support. It would, however, be necessary to attract other lenders, including institutions. SFCs may be able to do this if the maturity pattern of their bonds were biased in favour of shorter maturities; they can even float bonds of different maturities, the shorter maturity bonds for banks and individuals and the longer ones for institutions like LIC, trusts, etc. Apart from this argument from the point of view of resources, even from the point of view of the business of these Corporations, it appears that the introduction of shorter maturity bonds would correspond more with the pattern of their business. This argument would become clearer in the light of the following data relating to the time-pattern of outstanding loans and loans sanctioned as at the end of 1962; the time-pattern of outstanding loans is on the basis of number of years left for repayment as at the end of 1962, and of sanctions on the basis of the repayment schedules specified in the sanction letters.

	% of total for					
	Less than 3 years	Over 3 but less than 7 years	Over 7 but less than 10 years	Over 10 but less than 15 years	Over 15 years	Total
Outstandings	12	27	44	17	*	100
Sanctions	0.3	5	30	60	4.7	100

(*A very small sum is outstanding.)

III.33. Since the business of these Corporations has gathered certain momentum only in the last three to four years, the two patterns should be broadly similar if the sanction pattern remained the same from year to year. But the two patterns diverge considerably, indicating that probably in the earlier years sanctions were biased more in favour of shorter repayment schedules than in the case of sanctions in recent

years, which probably dominate the pattern of sanctions. This may also have happened as big loans, of upto Rs. 20 lakhs instead of upto Rs. 10 lakhs, to public limited companies and co-operatives, have been sanctioned only since April, 1962, and these are likely to be of longer maturity than the earlier loans. This is also corroborated by the wide gap between sanctions and outstanding loans of SFCs for the maturity period of 10-15 years. This gap is wider for the figures of SFCs and MIIC taken together, as the proportion of bigger loans to medium and large-sized industrial units to the total is higher in the case of MIIC than for SFCs (cf. Appendix).

III.34. If then the trend toward longer maturity loans is of recent origin, the time-pattern of outstanding loans may diverge, for a number of years, from that for loans sanctioned. It may take about fifteen years before the two patterns are more or less similar. During this period, the maturity pattern of outstanding loans would be more or less similar to the average of the two maturity patterns as shown below—

	% of total for		
	Upto 7 years	7-10 years	Over 10 years
Outstandings	39	44	17
Sanctions	5	30	65
A middle pattern	25	35	40

In the light of this likely pattern, it appears that about a quarter of the total loans would be for periods of upto 7 years. It would, therefore, be advantageous to borrow funds from the market to this extent by floating bonds of maturity of 7 years or less; interest on such borrowing would also be fractionally below that for borrowing for longer periods. If precedent is wanted for this suggestion, one can cite the Long-Term Credit Bank of Japan. As at the end of 1962, over 82 per cent of its loans of over $1.1 billion were for over 5 years; but this was financed by the issue of (*a*) interest-bearing debentures of 5 years maturity, and (*b*) discount debentures of one-year maturity, latter amounting to a quarter of the outstanding as on 31st March, 1962. Both these debentures are issued monthly to avoid having idle funds.

III.35. As SFCs function in a capital market which does not bear close resemblance with that of Japan, the shorter-dated bonds could be supplemented with longer-dated ones which would be taken up by certain important classes of institutional investors. In this connection, the innovation of rural debentures in the agricultural credit sector may be mentioned:—land mortgage banks, which sanction long term loans for agricultural improvements, issue these debentures in two lots—one with a maturity of 7 years and offered to individuals, and another with a

maturity of 15 years, offered to Reserve Bank. Repayments of loans received in the first seven years are accumulated to repay the first lot, and those received in the next eight years to repay the second lot. In the last three years, about Rs. 5 crores of such debentures have been floated and subscribed to.

Borrowings from Reserve Bank and Refinance Corporation for Industry

III.36. The outstanding borrowings of the Corporations from Reserve Bank and RCI as on 31st March, 1963, are given below. All the borrowings (except Rs. 5 lakhs of Maharashtra Corporation) from Reserve Bank were only against Government securities. No SFC had any outstanding borrowing from the State Government at the end of March, 1963.

Borrowings of Corporations from RBI and RCI as on 31-3-1963.

(Rs. lakhs)

Corporation of	RBI	RCI
1. Rajasthan	8.00	—
2. Maharashtra	47.00	33.05
3. Madhya Pradesh	17.40	—
4. Madras	—	111.22
5. Punjab	—	15.20
Total	72.40	159.47

An on the last Friday of September, 1963, borrowings from Reserve Bank by SFCs stood at Rs. 164.55 lakhs. On 30th September, 1963, SFCs and MIIC had outstandings of Rs. 150.16 lakhs and Rs. 120.87 lakhs respectively from RCI.

III.37. Borrowings from Reserve Bank for 90 days on trustee securities or for 18 months against special bonds or trustee securities, are designed mainly to act either as interim finance—to be used pending a more opportune time for floating bonds, or as shock absorbers—to meet repayment obligations of bonds at a time when defaults by borrowers have upset the SFC's cash flows or market conditions are unfavourable to liquidate security holdings to realise cash. Borrowing for 18 months is at present statutorily limited to 60% of the paid-up capital of a SFC. It is suggested that this limit may be fixed at 100% of the paid-up capital as, unlike co-operative land mortgage banks, these Corporations do not have access to State Bank or its subsidiaries for temporary accommodation under State Government guarantee.

III.38. Although term borrowing from RCI does not partake of the same interim finance character as that from Reserve Bank, SFCs cannot,

as things stand at present, and even perhaps should not, depend much on this source for funds. They cannot, because, to distribute widely the benefits of its refinancing facilities, RCI has adopted a working rule not to lend to any SFC more than its paid-up capital and reserves; in a few cases it is relaxed upto twice that limit. They perhaps should not, because such facilities are designed primarily to induce institutions which specialize in the provision of short term funds to industry to explore the new, and in many ways more exciting, field of formal term lending. So the greatest claim on such resources as RCI can gather together should be from commercial banks and like institutions, and not from development banks like SFCs. Latter should provide term finance to industrial units by mobilising necessary resources from the public—an assignment which gains added significance in the context of the present economy of India where, as a result of the sizable and continuous deficit financing by the State, considerable incomes are being generated, some portions of which must be syphoned off to reduce their inflationary potential.

III.39. There is often a demand that Reserve Bank may assist SFCs under Section 17(2) (bb) of the Reserve Bank Act, under which a State co-operative bank or a SFC can get reimbursement from Reserve Bank for periods upto 12 months in respect of its advances to cottage and small scale industries for financing production or marketing. But such advances have to be against bills and promissory notes which bear "two or more good signatures", the small scale units must belong to industries which are approved by Reserve Bank, and the State Government must fully guarantee the advances from Reserve Bank. The main object of introducing this Section in the Reserve Bank Act in 1953 was to facilitate advances to industrial co-operatives by State and central co-operative banks. But provision was then made for SFCs too in case they gave advances to units in such approved industries for working capital or marketing. So far only the handloom industry has been approved for this sub-section, and State co-operative banks are obtaining reimbursement from Reserve Bank against State Government guarantee and on the signature of themselves and of central co-operative banks. A few other industries have been studied by the Agricultural Credit Department to determine their eligibility for being approved by Reserve Bank, but none has made the grade. Current thinking in the Bank is that no further industries need be approved; State and central co-operative banks may finance industrial co-operatives out of their own resources, protecting themselves with the guarantee under the Guarantee Scheme. If this hampers provision of rural credit, the Bank would consider the matter when fixing the limit for such credit. Thus, in the co-operative sector, handloom weavers belonging to co-operatives can obtain finance from co-operative banks under Section 17(2)(bb). For weavers outside the co-operative fold, recourse cannot be had to this provision by SFCs as State Governments are not prepared to extend their

guarantee as required under this Section and the second signature, apart from that of the SFC, will be difficult to provide for this sector. As matters stand, therefore, SFCs cannot get any reimbursement finance from Reserve Bank under this Section, and it may be considered whether the provision should be deleted from the Reserve Bank Act. In any case, SFCs' advances for working capital are still meagre, and such advances are given along with term loans which will qualify for refinance from RCI.

Reserve Fund and other Reserves

III.40. In terms of Sec. 35 of the Act, a SFC is to establish a reserve fund, and continue to contribute towards such fund out of profits until it becomes equal to its paid-up capital, after which it can, of course, create other reserves. There is no statutory provision governing the proportion of profits to be appropriated to this fund, as is prescribed in the Banking Companies Act, 1949, or Co-operative Societies Act, 1912 (or similar State enactments/rules) for commercial banks and co-operative banks respectively. Although legislators may not have foreseen in 1951 that few SFCs would readily attain viability, the Act may not have provided for specific allocations to this fund as it may have been held that, in the initial years, SFCs would credit as much of the surplus as possible after meeting other commitments, and more would be credited later as the dividend was statutorily restricted to 5%. Such a restriction rarely applies to foreign development banks which may account for the frequent provision in their case relating to credits to such funds out of profits. Under the Monetary and Banking Law of Iran, the Industrial and Mining Development Bank of Iran is to transfer at least 15% of net profits to the legal reserve, until it equals the paid-up capital. The net profits of the Pakistan Industrial Credit and Investment Corporation are to be applied as follows— not less than 15% as reserve in the first instance; thereafter not less than 10% of the profits remaining after the distribution of dividend not exceeding 7% are to be set aside; further out of profits remaining after distribution of an additional dividend not exceeding 6%, not less than 50% are to be set aside as reserve.

III.41. The question of allocating a specified percentage of profits to the reserve fund was considered at the Sixth SFCs' Conference, 1959, at the instance of Reserve Bank. The Conference held that no definite percentage need be fixed, for any allocation to reserves would have the effect of increasing the subvention from State Government for dividends as no SFC had then reached the stage of being able to pay dividends out of the net post-tax profits. But this consideration does not seem to have weighed when, according to the Finance Act, 1961, 10% of SFCs' annual profits were exempted from tax if set apart in a Special Reserve Account (discussed below). As yet, only three SFCs out of fourteen have reached the position of not having to draw subventions. For the rest, the creation of this special reserve has involved drawing more subventions.

III.42. In addition to this Statutory Reserve Fund, Sec. 35(A) of the Act as amended in 1962 provides for the creation of a Special Reserve Fund out of the dividends which the State Government and Reserve Bank may forgo. Further, the Indian Finance Act, 1961, permitted the setting up of a Special Reserve Account to which a specified fraction of the net profit can be credited, tax free, upto a ceiling amount. The various reserves of SFCs are reviewed below:

(*i*) Statutory (General) Reserve—Table III shows the quantum of statutory and other reserves built up by SFCs as on 31st March, 1963. During 1962-63, appropriations to the Statutory (General) Reserve Fund aggregated only Rs. 0.92 lakh. Major contributors towards this sum were Mysore, Madhya Pradesh, Kerala, Uttar Pradesh and Maharashtra SFCs. The total amount in this Fund of the fourteen SFCs as on 31st March, 1963, was only Rs. 13.07 lakhs. Andhra Pradesh, Assam, Kerala, Maharashtra, West Bengal and Madhya Pradesh SFCs contributed the bulk of this total.

(*ii*) Special Reserve Account for purposes of Section 36(1) (viii) of the Income Tax Act, 1961—The Finance Act, 1961 provided that approved term lending institutions could annually credit a maximum of 10% of their total income to a Special Reserve Account, till the total credits equal the paid-up capital; the amounts so credited would be exempt from tax. This is a welcome concession, but its effect is as yet meagre as most SFCs are not making sizable profits. Actually, as many of them are drawing subventions from the States to pay dividends, credits to this Account would mean pro tanto drawing more subventions. During 1962-63, SFCs contributed a sum of Rs. 7.23 lakhs to this Special Reserve, and as on 31st March, 1963, they had altogether Rs. 15.25 lakhs in this Special Reserve Account. If the limit of this concession, viz., 10% of annual profits, is enhanced, it will help to improve the finances of these institutions faster by strengthening their reserves. As long as the total transfers to the Account are limited to the paid-up capital, there would be hardly any real loss of revenue to Government, which might even conceivably gain by allowing faster accumulations now, by increasing SFCs' profit-earning capacity; and if the rate of Corporation tax increases in the future, Government will collect higher revenues earlier than before. This point is discussed again in a later Section.

(*iii*) Special Reserve Fund under Section 35A of the State Financial Corporations Act as amended in 1962—As a result of guaranteed dividends and low profits, SFCs have had to draw subventions from the States to the extent of Rs. 1.62 crores as on 31st March, 1963, to meet the guaranteed dividend liability. On this same date, the State Governments and Reserve Bank held respectively 46.3% and 17.5%, aggregating 63.8%, of their total paid-up capital of Rs. 14 crores. Since inception, SFCs have paid to the State Governments and Reserve Bank together a sum of approximately Rs. 2.36 crores as dividends on

TABLE III

Quantum of reserves built up by State Financial Corporations and the Madras Industrial Investment Corporation Ltd. as [redacted] 31st March, 1963 (including appropriations from profits for the year 1962/63).

(In Rupees)

Corporation of	Statutory Reserve Fund	Special Reserve Account	Special Reserve Fund (Sec. 35A)	Other reserves		
				Investment reserve	Reserve for bad and doubtful debts.	Others
(1)	(2)	(3)	(4)	(5)	(6)	(7)
1. Andhra Pradesh	2,16,800	1,96,340	—	5,000	50,000	—
2. Assam	1,70,000	89,653	—	—	—	—
3. Bihar	53,930	72,050	—	—	—	—
4. Gujarat	[redacted]	87,740	1,05,000	35,000	34,416	—
5. Jammu & Kashmir	9,333	17,333	—	7,491	—	—
6. Kerala	1,76,257	1,53,518	1,05,000	—	—	—
7. Madhya Pradesh	1,00,000	1,03,000	52,500	27,000	—	—
8. Maharashtra	1,73,227	1,88,057	—	79,018	26,578	—
9. Mysore	73,762	50,000	—	—	—	941
10. Orissa	25,000	66,000	70,000	33,000	10,000	—
11. Punjab	62,000	1,44,600	—	88,400	—	—
12. Rajasthan	22,000	1,28,300	1,00,000	—	16,000	—
13. Uttar Pradesh	70,000	80,000	1,05,000	—	—	—
14. West Bengal	1,54,796	1,48,750	1,40,000	—	—	—
Total of 14 SFCs	13,07,187	15,25,341	6,77,500	2,74,909	1,36,994	941
15. Madras	2,00,000	1,61,976	—	4,05,000	1,25,000	—
Total of 15 Corporations	15,07,187	16,87,317	6,77,500	6,79,909	2,61,994	941

NOTE: 1. Special Reserve Fund under Section 35A has been created out of dividends forgone by the concerned State Governments and Reserve Bank

2. All these do not figure in the Balance Sheets as on 31st March, 1963 of all State Financial Corporations as appropriations in some cases are included after Annual General Meetings.

3. In the case of Madras Industrial Investment Corporation, the figures do not include appropriations for the year 1962-63.

their shareholdings. Thus, the State Governments were accepting dividends on their shares in SFCs, and to meet the dividend liability the latter were drawing subventions from the States.

In the attempt to remedy this peculiar situation, Sec. 35A was introduced in the SFCs Act in 1962 whereby a Financial Corporation may establish a Special Reserve Fund and transfer to it such portion of the dividends accruing to the States and Reserve Bank as these two parties may fix by mutual agreement. But the total amount in this Fund is not to exceed 10% of the paid-up capital, and no shareholders except Reserve Bank and the State Government will have claim to this Fund. The Bank advised the States that it would be willing to forgo a part or whole of the dividend due to it if the respective State Governments also agreed to forgo similar amounts. Details of dividends forgone or agreed to be forgone upto 31st March, 1963 by State Governments and the Bank are shown below—

1961-62: Forgone or agreed to be forgone by RBI (Rs.)	1962-63: Agreed to be forgone by RBI (Rs.)	Corporation of	1961-62: Forgone or agreed to be forgone by State Government (Rs.)	1962-63: Agreed to be forgone by State Government (Rs.)
52,500	70,000	(1) Gujarat	52,500	70,000
52,500	—	(2) Uttar Pradesh	52,500	—
52,500	52,500	(3) Kerala	52,500	52,500
35,000	—	(4) Orissa	35,000	—
—	40,000	(5) Jammu & Kashmir	—	40,000
—	70,000	(6) Andhra Pradesh	—	70,000
—	60,000	(7) Mysore	—	72,000*
50,000	50,000	(8) Rajasthan	50,000	50,000
70,000	—	(9) West Bengal	70,000	—
—	52,500	(10) Madhya Pradesh	52,500	52,500
3,12,500	3,95,000	Total	3,65,000	4,07,000

(*It may be stated that the dividend agreed to be forgone by Mysore Government for 1962-63, viz., Rs. 72,000 is less than one-half of the total dividend due to it, whereas the Reserve Bank's contribution of Rs. 60,000 represents the entire dividend due to it on its shareholding.)

On the basis of the dividends forgone by State Governments and the Reserve Bank of India during 1962-63 (so far), it would take—on the average—about 9 years to reach the ceiling of 10% of paid-up capital. If these two major holders agree to forgo the entire claim, it would take only about 5 years to reach the limit of 10% of the paid-up capital (cf.

Table IV). This limit of 10%, we shall suggest later, may be raised to 25% to strengthen the reserves of SFCs, which would enhance their profit earning capabilities as well as enable them to take more calculated risks in their loans and advances, aided by a competent technical staff for scrutiny and follow-up work.

(*iv*) Reserve Fund for Bad and Doubtful Debts—During 1962-63, only two SFCs contributed Rs. 26,000 to this Fund. The aggregate amount under this head as on 31st March, 1963, was only Rs. 1.37 lakhs.

(*v*) Investment Reserve—During 1962-63, five SFCs made a provision aggregating Rs. 1.01 lakhs towards this reserve. The total amount of such reserves built up by all SFCs was barely Rs. 2.75 lakhs.

III.43. Thus, the total reserves of all SFCs as on 31st March, 1963, were as follows:

	(Rs. lakhs)
(*i*) Statutory Reserve	13.07
(*ii*) Other Reserves:	
(*a*) Investment Reserve	2.75
(*b*) Reserve for bad and doubtful debts	1.37
(*c*) Special Reserve Account	15.25
	32.44

In addition, under Sec. 35A of the Act, the accretion to reserves out of dividends forgone by Reserve Bank and the State Governments would amount to Rs. 6.78 lakhs during 1961-62. Thus, the total reserves as on 31st March, 1963 would be of the order of Rs. 39.22 lakhs or only 2.8% of the paid-up capital of Rs. 14 crores and an even smaller proportion of loans—sanctioned: Rs. 46 crores, and outstanding: Rs. 25 crores. Reserves are, thus, very meagre.

III.44. As on 30th June, 1962, MIIC had built up General Reserves of Rs. 2 lakhs and its Special Reserve, Investment Reserve and Reserve for Bad and Doubtful Debts stood at Rs. 1.62 lakhs, Rs. 4.05 lakhs and Rs. 1.25 lakhs respectively. Thus, the aggregate reserves stood at Rs. 8.92 lakhs, which was about 6.7% of the paid-up capital of Rs. 132 lakhs.

Concluding observations

III.45. Thus, the resources position of SFCs as at the end of 1962-63 seems to be as follows:—They have, altogether, equity resources of Rs. 14 crores, of which nearly Rs. 9 crores have come from the State Governments and Reserve Bank. Deposits and reserves are exceedingly meagre. They have borrowed from the market about Rs. 16 crores against bonds, and another Rs. 1.21 crores from Reserve Bank and RCI. To complete the picture, mention should be made of the fact that from

TABLE IV

Statement showing tentative number of years required to build up Special Reserve Fund upto 10% of paid-up capital in terms of Section 35A of the State Financial Corporations Act, 1951.

(Rs. '000)

Corporation of	Shares held by		Rate of dividend	Dividends forgone by				No. of years for Fund to accumulate 10% of paid-up capital		
	State Government	Reserve Bank		State Government		Reserve Bank		On the basis of dividend forgone in 1961-62	On the basis of dividend agreed to be forgone in 1962-63	If entire dividend accruing to State Govt. and Reserve Bank are forgone
				1961-62	1962-63 (agreed)	1961-62	1962-63 (agreed)			
	Rs.	Rs.		Rs.	Rs.	Rs.	Rs.			
1. Andhra Pradesh	70,00.0	20,00.0	3½%	—	70.0	—	70.0	—	11	5
2. Assam	51,67.5	20,00.0	3½%	—	—	—	—	—	—	4
3. Bihar	40,00.0	15,00.0	3½%	—	—	—	—	—	—	6
4. Gujarat	36,00.0	20,00.0	3½%	52.5	70.0	52.5	70.0	10	8	6
5. Jammu & Kashmir	28,79.5	10,00.0	4%	—	40.0	—	40.0	—	7	4
6. Kerala	60,41.5	15,25.0	3½%	52.5	52.5	52.5	52.5	10	10	4
7. Madhya Pradesh	58,35.0	15,00.0	3½%	52.5	52.5	—	52.5	—	10	4
8. Maharashtra	32,82.5	18,04.5	3½%	—	—	—	—	—	—	6
9. Mysore	40,46.5	15,00.0	4%	—	72.0	—	60.0	—	8	5
10. Orissa	64,17.5	20,00.0	3¼%	35.0	—	35.0	—	15	—	3
11. Punjab	41,65.5	20,00.0	3%	—	—	—	—	—	—	6
12. Rajasthan	36,20.0	21,00.0	3½%	50.0	50.0	50.0	50.0	10	10	5
13. Uttar Pradesh	55,36.0	15,00.0	3½%	52.5	—	52.5	—	10	—	5
14. West Bengal	31,77.0	20,00.0	3½%	70.0	—	70.0	—	8	—	6
Total	6,47,68.5	2,44,29.5		3,65.0	4,07.0	3,12.5	3,95.0			
				Average number of years				11	9	5

time to time some SFCs have received funds from State Governments for giving small loans under the State Aid to Industries Acts/Rules. About Rs. 3 crores of such funds have so far been received and disbursed (none of the SFCs except that of Punjab, includes either these funds or the loans made out of them in the balance sheet). Thus, the resources of SFCs add up to Rs. 34 crores—Rs. 14 crores owned and Rs. 20 crores borrowed.

III.46. We saw above that the holdings of bonds of SFCs are not broad-based. Government have been moved more than once to include these bonds, which are trustee securities, as one of the securities in which provident fund accumulations could be invested. This would increase their attractiveness to institutional investors by improving their marketability. But Government have not agreed to this on the plea that provident fund accumulations of the concerns covered by the Employees Provident Fund Act, 1952, are invested in Central Government securities only as such monies have been included in the Central resources for the Plan. Every year substantial amounts are invested in trustee securities out of accumulations in provident funds covered by the Act of 1952 as well as other similar funds, particularly those of certain categories of employees in the public sector. These accumulations are now invested almost wholly in Central Government securities. We suggest that Government may agree that some part of the large annual flow of resources to these provident funds may be invested in the bonds that are floated by SFCs from time to time. Even if the flow of funds from provident funds has been counted as part of Central resources for the Plan (incidentally, such provision could only have been made in general terms as no detailed projections were made, which prevents us from knowing if such funds are contributing more than had been estimated), if only a part of such funds was permitted to be invested in SFC bonds which, by virtue of the guarantee of State Governments, rank as trustee securities, the resources position of Government perhaps would not be seriously affected. These bonds would also give a higher guaranteed yield to the funds than Central Government securities. Government may also recognise both bonds and deposit receipts of SFCs as approved securities under Sec. 11(2)(b) of the Income Tax Act, so that investments in them by charitable institutions would be exempt from income tax. Unless such measures are taken, the other alternative to improve the attractiveness of these bonds for the public would be to offer high yields. But as these bonds are guaranteed by State Governments, such a move may be opposed as tending to disrupt the rate structure for Government borrowings. Further, as SFCs are expected to finance small scale units at not too a high rate of interest, the move may also be opposed as a preliminary to pushing up lending rates which would affect small scale units. But some solution to this problem should, however, be found. In the case of IFC, large sums have been lent to it by the Government of India. Thus, at the close of 1962-63, IFC had received from

Government about Rs. 25 crores, mostly at $4\frac{1}{2}\%$ interest, when its paid-up capital was Rs. 7 crores, and bonds outstanding—Rs. 28 crores. It is necessary that provision should be made for similar loans to these Corporations to supplement what they can raise from the market, including LIC and various provident funds, against bonds. Alternatively, Reserve Bank should come to the rescue of SFCs which find it difficult to raise funds from the market at rates approved by the Bank. Being a central bank it cannot in the normal course lend for long term. We, therefore, recommend that a long term operations fund may be created by the Bank on the lines of the National Agricultural Credit (Long Term Operations) Fund (Section 46A, Reserve Bank of India Act). This Fund is utilised for providing the State co-operative and central land mortgage banks with medium term and long term loans and for purchase of land mortgage bank debentures*. Industry is no less important than agriculture and SFCs which have been set up to foster industrialisation in the difficult sector of small and medium industries can claim the same preferential treatment as State co-operative banks and central land mortgage banks. The proposed fund which may be termed "The National Industrial Credit (Long Term Operations) Fund" will not only enable Reserve Bank to put on a formal footing its purchases of SFCs shares —at present above Rs. 2.44 crores, and its contributions to their bonds; it will, additionally, enable the Bank to offer a substantial measure of assistance to SFCs' resources as well. We feel that such a step is essential as Government are genuinely concerned in aiding these institutions to fulfil the objectives for which they were set up.

III.47. As compared with many other similar institutions, both in this country, like IFC and ICICI, and elsewhere e.g., in the Philippines, Pakistan, Iran and Ceylon, SFCs have failed as yet to resort to two other major sources of funds—viz., borrowings in foreign currencies, and long term borrowings from the State on concessional terms. It was mentioned earlier that most foreign development banks, in the underdeveloped regions in particular, have secured loans in foreign currencies with which they can meet the foreign exchange needs of their borrowers. In India, too, we saw that, IFC and ICICI, as also NSIC, have such resources, and are continually trying to augment them from various sources. While dealing later with the loans and advances of SFCs, we shall have occasion to remark that, perhaps, one of the reasons why SFCs have not financed many units in the newly set-up industries, especially chemicals, mechanical and electrical engineering, etc. is their lack of foreign exchange resources to be lent to borrowers for the import of machinery, etc; ICICI, on the other hand, has been able to divert a good portion of its resources to these newer industries as it could provide its borrowers with the necessary foreign exchange. If SFCs are to make a significant impact on our industrial development, especially in the sector

* So far Rs. 73 crores have been appropriated to this Fund and as on 30th June, 1963, outstanding loans from it amounted to Rs. 40.7 crores.

of small and medium-sized units, they should be enabled to meet the foreign exchange requirements of their clients. Participation arrangements with IFC and ICICI whereby these latter bodies will provide the foreign exchange for particular borrowers would not be a fully satisfactory solution to this problem. These latter institutions will ordinarily be interested only in relatively large transactions, while we would not certainly like to encourage the resources of SFCs being utilised for assisting larger units, to the neglect of small and medium-sized ventures.

III.48. Unlike again ICICI, as also the recently set-up Agricultural Refinance Corporation, and, to some extent, also RCI, the resources of SFCs have not been supplemented by funds obtained from the Government on concessional terms. Immediately after ICICI was registered in January, 1955, it received from Government of India an interest-free long term loan of Rs. 7.5 crores repayable in 15 equal annual instalments from the 16th year onwards. Also, and this may be without precedent, this loan ranks after the equity in the event of liquidation. Agricultural Refinance Corporation too has received a similar loan on identical terms, except the last, as this Corporation is largely State-owned and all its borrowings carry Government guarantee. RCI too has entered into an agreement with Government for funds to be obtained as loans, repayable by 1st July, 1997; the annual interest payable on the outstanding borrowings has been kept flexible, to be determined in the light of its earnings, the only proviso being that such payments will not exceed, in the aggregate, what would have been payable at a rate of 4%, simple interest.

III.49. As development banks, the business of which can only grow with time, it would have benefited SFCs greatly if they had access to such concessional funds in the early years of their working. Not that development banks elsewhere have invariably had this facility—though a few, both those owned privately as also Government banks, did get it. The Development Finance Corporation of Ceylon had obtained 30 years interest-free loans from Government. The Industrial and Mining Development Bank of Iran has secured very substantial loans from Government on identical terms and such borrowings are treated on terms pari passu with its equity capital. The Development Bank of the Philippines has arrangements for borrowing from the Government as also the Central Bank at rates ranging from 0% to 3% for various maturities. The Pakistan Industrial Credit and Investment Corporation obtained from Government an interest-free loan for 7½ years in 1957, followed by one at 4% for 36½ years. The Western Region Finance Corporation of Nigeria has borrowings from Government at 3½%.

III.50. In addition to such concessional funds, some foreign development banks have also obtained substantial amounts from Government from which they derive a large income in the shape of management fees e.g., the Industrial and Mining Development Bank of Iran gets 3% and the Industrial Development Bank of Turkey 4% on such funds annually

(cf. Chapter V below). In India this fee is only 2%, and that too, surprisingly enough, only in the first year that a loan is made; also the average size of loans given out of State funds is very small so that much of the energies of SFCs is consumed in handling an uneconomic line of business.

III.51. While SFCs received no such assistance, their statute compelled them to pay dividend on their shares right from the day they commenced business and received the shareholders' money. This seems unprecedented, and is especially surprising as the State Governments and Reserve Bank were the major shareholders. With the provision in the Act that the States would meet the deficit in net profits (after payment of Corporation tax) in relation to the guaranteed dividend liability, SFCs were at least saved from depleting their cash resources in meeting this liability. But, most of them are on the other hand, still creating a liability to the States for repaying this assistance, mortgaging, in effect, their future profits. Some recommendations are made later for ameliorating this state of affairs.

APPENDIX TO CHAPTER III

Periodwise breakdown of loans of SFCs and MIIC—outstandings and sanctions—as on 31st March, 1962

(Rs. lakhs)

Period	Size of Unit	SFCs		SFCs and MIIC	
		Outstandings	Sanctions	Outstandings	Sanctions
(1)	(2)	(3)	(4)	(5)	(6)
Less than 3 years	Small	47.49	4.36	54.53	4.36
	Others	76.58	10.35	300.34	10.35
Over 3 but less than 7 years	Small	120.91	59.64	129.75	59.64
	Others	350.05	163.20	634.05	178.20
Over 7 but less than 10 years	Small	384.12	314.56	387.38	332.87
	Others	822.55	742.27	882.44	1161.34
Over 10 but less than 15 years	Small	118.79	742.11	118.86	755.76
	Others	355.25	1949.32	361.28	2308.41
Over 15 years	Small	—	11.37	—	12.57
	Others	10.00	90.05	10.40	224.80
Total	Small	671.31	1132.04	690.52	1165.20
	Others	1614.43	2955.19	2188.51	3883.10
Grand Total		2285.74	4087.23	2879.03	5048.30

CHAPTER IV

DEPLOYMENT OF RESOURCES

Investments

IV.1. The policies and procedures which have governed the deployment of the resources of SFCs will now be considered under two broad heads—investments, and loans and advances. In terms of Sec. 34 of the SFCs Act, a SFC may invest its funds in the securities of the Central Government or of any State Government. Table V will show that as on 31st March, 1963, only Jammu & Kashmir SFC had invested Rs. 22.84 lakhs in Central Government securities. This, together with a small sum of Rs. 0.50 lakhs invested by West Bengal SFC in Defence Deposit Certificates, formed about 7.3% of the aggregate investments in Government securities and debentures of Rs. 320.49 lakhs. On this same date, ten other SFCs had investments in State Government securities of Rs. 274.85 lakhs, or 85.8% of the total investments. This may be because they are under pressure from the States to invest in State loans.

TABLE V

Investments of State Financial Corporations as on 31st March, 1963.

(Rs. lakhs)

Corporation of	Central Government	State Government	Debentures	Total
1. Andhra Pradesh	—	31.33	8.55	39.88
2. Assam	—	—	—	—
3. Bihar	—	5.12	—	5.12
4. Gujarat	—	18.64	3.75	22.39
5. Jammu & Kashmir	22.84	—	—	22.84
6. Kerala	—	20.03	—	20.03
7. Madhya Pradesh	—	21.91	—	21.91
8. Maharashtra	—	56.62	—	56.62
9. Mysore	—	—	10.00	10.00
10. Orissa	—	14.04	—	14.04
11. Punjab	—	38.01	—	38.01
12. Rajasthan	—	41.79	—	41.79
13. Uttar Pradesh	—	27.36	—	27.36
14. West Bengal	0.50*	—	—	0.50
Total	23.34	274.85	22.30	320.49
Percentage to Total	7.3	85.8	6.9	100.0

* Investment in 4½% Ten Year Defence Deposit Certificates.

IV.2. The maturity pattern of these investments as on 31st March, 1963, (Table VI), will show that investments of Rs. 5.03 lakhs in Central Government securities, Rs. 243.84 lakhs in State Government securities and Rs. 22.30 lakhs in debentures of industrial units, that is Rs. 271.17 lakhs, or about 84.6% of total investments of Rs. 320.49 lakhs of thirteen SFCs, were in securities maturing after 5 years. Four SFCs, viz., Bihar, Jammu & Kashmir, Madhya Pradesh and Punjab—had invested an amount of Rs. 49.32 lakhs (15.4% of the total) in securities of the Central Government and State Governments maturing within 5 years. SFCs in Assam and Mysore had no investments in Central or State Government securities; their surplus funds were kept in deposits with banks (in consultation with Reserve Bank).

IV.3. In December, 1956, Central Government after consulting Reserve Bank, issued instructions to States about the investment of surplus funds by SFCs. It was felt desirable to maintain a working balance in short term deposits with banks upto about a year's requirement of funds. It was stressed that investment in long-dated securities would be unsuitable and that it would be the best policy for SFCs to invest in short-dated Government securities of not more than 2 to 3 years' maturity, in consultation with Reserve Bank. The State Governments were requested that in case they saw no objection to this, they may instruct SFCs under Sec. 39(1) of the Act in terms of Central Government's letter.

IV.4. A review in September, 1961, revealed that only eight States, viz., Uttar Pradesh, Rajasthan, Orissa, Punjab, Kerala, Madhya Pradesh, Jammu & Kashmir and Gujarat had issued such instructions. Some of these had later permitted their SFCs to invest in medium-dated securities. Partly as a result of this, it was seen that ten out of fourteen SFCs had invested in such securities. It was then thought that Reserve Bank might take up the issue with the concerned States. But as the SFCs Act was then about to be amended, enabling SFCs to borrow, for periods upto 18 months, from Reserve Bank against Government securities as well as their own bonds [Sec. 7(2)(*b*)], the matter was not pursued further. The general rise in interest rates (on bank deposits, etc.) with its effects on yield pattern is bound to affect the gilt-edged market also; and it will be felt more in the long-dated sectors. Thus, to avoid capital depreciation and losses if some of these investments need to be liquidated to replenish cash resources, as far as possible SFCs should invest in short-dated securities.

IV.5. As compared with development banks elsewhere, there appear to be two major lacunae in the investments of SFCs, viz., the absence of equities and debentures of industrial concerns. Thus, on 31st March, 1962, the Development Finance Corporation of Ceylon had invested Rs. 2.9 million in equities; the China Development Corporation is authorised to use its surplus funds to assist new private industries by investing in their shares, within certain limits; the Industrial and

TABLE VI

Statement showing maturity pattern of investments of State Financial Corporations as on 31st March, 1963.

(Rs. lakhs)

Corporation of	Maturing within 5 years		Maturing after 5 years			Total
	Central Government	State Government	Central Government	State Government	Debentures	
1. Andhra Pradesh	—	—	—	31.33	8.55	39.88
2. Assam	—	—	—	—	—	—
3. Bihar	—	0.15	—	4.97	—	5.12
4. Gujarat	—	—	—	18.64	3.75	22.39
5. Jammu & Kashmir	18.31	—	4.53	—	—	22.84
6. Kerala	—	—	—	20.03	—	20.03
7. Madhya Pradesh	—	10.00	—	11.91	—	21.91
8. Maharashtra	—	—	—	56.62	—	56.62
9. Mysore	—	—	—	—	10.00	10.00
10. Orissa	—	—	—	14.04	—	14.04
11. Punjab	—	20.86	—	17.15	—	38.01
12. Rajasthan	—	—	—	41.79	—	41.79
13. Uttar Pradesh	—	—	—	27.36	—	27.36
14. West Bengal	—	—	0.50	—	—	0.50
Total	18.31	31.01	5.03	243.84	22.30	320.49
Percentage to Total	5.7	9.7	1.6	76.1	6.9	100.0

Mining Development Bank of Iran, which may invest in the shares of any one enterprise upto 10% of the paid-up capital of the bank plus reserves subject to the total investments of 30% of the paid-up capital and reserves, had invested upto 20th March, 1962, Rials 45 million in shares of companies; the Pakistan Industrial Credit and Investment Corporation had, as on 31st December, 1962, almost a third of its investments of Rs. 47 million (book value) in equities of companies; the Western Region Finance Corporation of Nigeria, a statutory body, had, as on 31st March, 1961, invested over £1.5 million in equities. In most of these cases, investment in equities has been perhaps mainly of the nature of direct participation. In some—though fewer cases—it is also the result of taking up shares in fulfilment of underwriting obligations.

IV.6. Under Sec. 25(1)(*g*) of the Act, a SFC may subscribe to the debentures of an industrial concern, repayable within 20 years from the date of subscription. Sec. 25(1)(*f*) also permits a SFC to underwrite issues of stocks, shares, bonds and debentures of industrial concerns and to retain them, if this is necessary to fulfil underwriting obligations, upto 7 years. For retention after seven years, prior permission of Reserve Bank is necessary. As on 31st March, 1963, only three SFCs, of Andhra Pradesh, Mysore and Gujarat, had investments in debentures under Sec. 25(1)(*g*) for Rs. 8.55 lakhs, Rs. 10 lakhs and Rs. 3.75 lakhs respectively aggregating Rs. 22.30 lakhs representing about 1% of total loans of SFCs outstanding on that date. The provision under Sec. 25(1)(*f*) has so far been used independently by only Rajasthan SFC. This is discussed in Chapter V. There have also been two cases of underwriting in participation with other agencies, which are also discussed there. SFCs are not permitted to participate directly in the equities of companies.

IV.7. SFCs have thus played a negligible part in financing long term capital through debentures. In India, equity capital constitutes a very substantial part of the total capital raised by industry; preference shares and debentures are much less important. A recent study of the finances of 685 medium and large public limited companies conducted by Reserve Bank revealed that in 1960 and 1961, these companies had paid-up capital amounting to Rs. 318,63 lakhs and Rs. 339,24 lakhs respectively. Their debenture capital was Rs. 34,50 lakhs and Rs. 35,10 lakhs i.e. only about 10.8% and 10.3% respectively of the equity capital. Thus, the ability of SFCs, or for that matter, of the other long term lending agencies, to finance longer term needs of industry through purchase of debentures is narrowly limited by the small amount of debentures currently outstanding. The ability of SFCs to finance debenture issues becomes still more difficult because the smaller companies with which they generally deal are often unable to raise funds in the open market. Further, a large number of their clientele are non-corporate bodies; these cannot borrow through debentures. Another important factor which discourages this operation is the absence as yet of a broad-based

market for debentures. To serve the purpose of broadening the existing and potential investor-participation in industry, SFCs should finance equities and debentures. But to enable them to do so effectively, they should be able to revolve their portfolio of securities so that newer enterprises can be assisted. If they cannot, sooner or later, find a buyer, their funds would be blocked, adversely affecting their profit earning capacity.

IV.8. Despite this handicap, the role of SFCs, which are development banks, in financing long term capital through debentures and participation in equities cannot be overemphasised. Sooner or later, they must develop this business if they are to contribute their share towards developing a capital market. Apart from this, equity rather than loan is often the most appropriate form of financing a new enterprise or a rapidly expanding one, on which a fixed debt beyond a certain level might place an intolerable burden. Equity investments also enable the participating credit institution to share in the profitability of successful enterprises, thereby adding to its income and providing a cushion against possible losses on other investments. We, therefore, consider that the SFCs Act should be amended to authorise SFCs to directly participate in the equity of corporate industrial units. They should also devote more effort to develop debenture financing. No doubt, in the first few years, SFCs would not be able to participate in equity to any significant extent as it is a risky undertaking; so long as they are not able to build up adequate reserves, the regular and immediate income generated by a loan portfolio would naturally have a greater appeal to them than the delayed and uncertain returns on equity investments. We are suggesting elsewhere certain measures to strengthen their reserves and earning capacity, which would pave the way for undertaking this business. We also make the following suggestions to enable them to develop equity financing business gradually.

(a) Investments in, or underwriting of, debentures

IV.9. In the initial stages, SFCs should take up this operation in participation with IFC/ICICI, which would enable them to take advantage of the expertise already acquired by these larger institutions, and to increase the volume of their turnover. Further, since the cost of processing the applications, which will be shared by the participating institutions, will be relatively small, the revenues of SFCs will increase more than proportionately to the cost. They will gain necessary experience which will enable them later to take up this operation independently.

(b) Equity financing

IV.10. As stated earlier, the Act will require to be amended before this operation could be undertaken by SFCs. Although equity financing is most appropriate for new enterprises since, unlike a loan, it imposes no repayment or interest burden, in the initial stages SFCs cannot be expected to finance new ventures because of the risk involved and should

proceed cautiously. It will, therefore, be desirable for them to make a beginning by participating in equities of enterprises which have already become seasoned and with which they have had satisfactory dealings as lenders for a fairly long time. If more capital is needed for expansion, the enterprise may prefer to have it in the form of equity—which gives it a broader base on which to borrow from other sources, and might require the support of the SFC in issuing it. If SFCs participate in the equity, they will be able to share in the profits of growing enterprises.

IV.11. After acquiring sufficient experience, SFCs could later consider undertaking equity financing in respect of new ventures to fulfil their role of development banks.

IV.12. It may also be desirable to fix a ceiling, say 30% of the capital and reserves, upto which each SFC may engage in this business in the initial stages.

(c) Cash balances

IV.13. Under Sec. 33(2) of the SFCs Act, the funds of SFCs shall be deposited in Reserve Bank, or the State Bank of India and its subsidiaries or, in consultation with Reserve Bank, in a scheduled bank, or a State co-operative bank. The need for such deposits arises because SFCs must maintain a certain optimum relationship between their liquid and profit-earning assets. They have to keep liquid a sum adequate to meet all possible disbursals of sanctioned advances from time to time. They have also to pay, at regular intervals, interest on their bonds and other borrowings. It is necessary to find suitable employment for the balance of the funds in hand. As is well known, after advances, investments constitute the next most remunerative assets of the Corporations. If the demand for loans increases, they may liquidate some investments. Table VII shows that as on 31st March, 1963, SFCs had liquid resources, cash-in-hand and balances with commercial banks, etc., aggregating Rs. 443.69 lakhs (as against investments in Government securities aggregating Rs. 320.49 lakhs). Two SFCs—Assam and Mysore—which had large cash balances as on 31st March, 1963—as pointed out earlier, had no investments in Government securities on that date. There has been criticism in some quarters from time to time that large funds remain idle with some SFCs in cash or in securities, while there is a great demand for loans from industrial units, particularly the small scale units. To some extent, such funds are not really idle. They may be drawn upon at any moment by borrowers who have not utilized any or a part of the amounts sanctioned to them. This lag in disbursement as compared with sanctions may be dealt with by all SFCs levying a commitment charge on undrawn balances.

IV. 14. Though some SFCs may still not be able to deploy their resources with the maximum efficiency (we take up this matter again later), the recent amendment of the SFCs Act which permits them to borrow from Reserve Bank for periods upto 18 months [Sec. 7(2)(*b*)]

TABLE VII

Statement showing cash in hand and the balances of State Financial Corporations and MIIC with banks as on 31st March, 1963.

(Rs. lakhs)

Corporation of	Cash in hand	Balances with		Total
		Reserve Bank of India	Scheduled and State co-operative banks	
Andhra Pradesh	—	0.02	17.16	17.18
Assam	0.04	2.20	69.03	71.27
Bihar	0.15	—	35.84	35.99
Gujarat	—	—	16.09	16.09
Jammu & Kashmir	—	—	19.52	19.52
Kerala	0.37	—	38.75	39.12
Madhya Pradesh	0.42	0.08	2.99	3.49
Maharashtra	0.04	—	2.75	2.79
Mysore	—	0.01	104.52	104.53
Orissa	0.08	0.28	21.29	21.65
Punjab	0.03	0.19	32.06	32.28
Rajasthan	—	—	0.96	0.96
Uttar Pradesh	0.01	0.02	56.47	56.50
West Bengal	—	4.01	18.31	22.32
Total of SFCs	1.14	6.81	435.74	443.69
Madras*	0.01	—	3.22	3.23
Total of 15 Corporations	1.15	6.81	438.96	446.92

* As on 29th March 1963.

as also to obtain refinance from RCI [Sec. 7(4)] will make it possible for them to work with smaller margin of ready funds. However, as a further solution to this problem, it is suggested that SFCs having idle funds may, instead of investing in Government securities and bank deposits at low rate of interest, lend them to other needy SFCs, at a rate of interest at which the funds had been borrowed or even a slightly higher rate. Such inter-corporation loans might be for short terms, not exceeding one year, which would give the borrowing SFC time to raise other resources and would avoid the situation in which some SFCs are des-

perate for more resources while others have relatively large amounts of idle resources on which they earn interest at a lower rate than they have to pay on their borrowings. If necessary, the Act may be amended to give effect to this suggestion.

Loans and Advances

IV.15. During the quinquennium ended March, 1962, the total outstanding loans and advances of SFCs increased by a little over Rs. 14 crores to Rs. 18.65 crores. Over one-half of this increase was achieved in the last two years 1960-61 and 1961-62, largely by Maharashtra, Bihar, Punjab and Assam SFCs, each of which showed increases of almost a crore or more in these two years. In 1962-63, total outstandings increased by Rs. 6 crores to Rs. 25 crores, i.e. by 33% over 1961-62 end, while 1961-62 had shown an increase of 40% over 1960-61 end. In the five years ended 30th June, 1962, MIIC increased its loans and advances by Rs. 3.49 crores to Rs. 4.81 crores.

IV.16. Increases of this order by as many as 14 SFCs functioning over almost the entire country would be considered meagre by most standards. In the quinquennium ended 30th June, 1962, IFC's loans increased by almost Rs. 28 crores or an average of Rs. 5.6 crores a year, and in 1962-63, they rose by another Rs. 10 crores, excluding assistance in the shape of underwriting, guarantees, etc.

(a) Applications received and sanctioned, etc.

IV.17. The number and value of applications received by SFCs and MIIC during 1959-60 to 1961-62 have shown progressive increases:

	1959-60		1960-61		1961-62	
	No.	Amount (Rs. lakhs)	No.	Amount (Rs. lakhs)	No.	Amount (Rs. lakhs)
Total of 14 SFCs	479	1072.76	966	1680.95	1,193	2079.55
MIIC	25	112.25	44	409.44	48	503.68
Grand Total	504	1185.01	1,010	2090.39	1,241	2583.23

Maharashtra SFC reported the largest increase in respect of applications received—58 in 1959-60, 150 in 1960-61 and 409 in 1961-62. The amounts which these applications represented also recorded a considerable—though not parallel—increase—from Rs. 189.40 lakhs to Rs. 466.76 lakhs. Others showing similar increases were Andhra Pradesh, Madhya Pradesh, Punjab and West Bengal. In these three years, MIIC too had been receiving applications for increasingly large amounts.

IV.18. Of the applications received, the actual sanctions are as below, again both for SFCs and MIIC:

	1959-60		1960-61		1961-62	
	No.	Amount (Rs. lakhs)	No.	Amount (Rs. lakhs)	No.	Amount (Rs. lakhs)
Total of 14 SFCs.	254	524.29	488	859.26	674	1150.26
MIIC	16	63.66	16	122.98	27	296.72
Grand Total	270	587.95	504	982.24	701	1446.98

Thus, during each of these three years, the numbers of applications sanctioned by SFCs were only about 53%, 47% and 56% respectively of those received. The increase in sanctions over the three years was greatest in the case of Maharashtra SFC, followed by Andhra Pradesh, Madhya Pradesh, Mysore, Punjab and West Bengal. In the case of Kerala SFC, sanctions fell from 13 in 1959-60 and 19 in 1960-61 to only 9 in 1961-62, largely due to the enactment of the Kerala Agrarian Relations Act which made most of the landed properties in the State unacceptable as security. Similarly, Uttar Pradesh also recorded a drop from 18 in 1959-60 and 27 in 1960-61 to 14 in 1961-62.

IV.19. Cumulative figures of loans sanctioned by the Corporations at the end of each year are shown below:

	1959-60 (Rs. lakhs)	1960-61 (Rs. lakhs)	% increase of 1960-61 over 1959-60	1961-62 (Rs. lakhs)	% increase of 1961-62 over 1960-61
Total of 14 SFCs	2259	3057	35	4155	36
MIIC	539	662	23	958	45
Grand Total	2798	3719	27	5113	27

The total amount of loans sanctioned (cumulative) increased by 27% in each of the two years 1960-61 and 1961-62 over the previous year. All Corporations showed an increasing trend of loans sanctioned with the older Corporations of Madras, Maharashtra, Punjab, Uttar Pradesh and West Bengal registering substantial increases.

IV.20. The position in respect of total loans disbursed (cumulative) is shown below as at the end of each year:

	1959-60 (Rs. lakhs)	1960-61 (Rs. lakhs)	% increase of 1960-61 over 1959-60	1961-62 (Rs. lakhs)	% increase of 1961-62 over 1960-61
Total of 14 SFCs	1349	1750	30	2430	39
MIIC	475	555	17	704	27
Grand Total	1824	2305	20	3134	27

Cumulative disbursements increased by 20% in 1960-61 and by 27% in 1961-62. Largest disbursements were reported in the case of Madras, Maharashtra, Punjab, West Bengal and Kerala Corporations.

IV.21. During the three years, altogether 141, 177 and 353 applications were withdrawn while 81 applications for Rs. 170.76 lakhs, 113 for Rs. 267.16 lakhs and 134 for Rs. 255.95 lakhs were rejected by the Corporations.

IV.22. Rejected applications formed 15%, 10% and 10% respectively of all applications received in these years. Orissa SFC had most rejections, followed by West Bengal, Uttar Pradesh and Madras, for a wide variety of reasons, the main ones being:

(1) Scheme not feasible—technically and financially; (2) inadequate creditworthiness of borrower; (3) past record not encouraging; (4) inadequate security; (5) unsatisfactory title to security; (6) difficult position of raw materials; (7) low priority for certain industries (viz., for rice, dal, khandsari sugar) due to excess capacity; (8) sizable amount already advanced to the industry; (9) against Corporation's policy; (10) uneconomic nature of the unit; (11) other reasons—adverse reports from Directors of Industries, litigation against party, party not showing interest, or trying to defraud the Corporation, etc. Most applications were rejected due to reasons listed at (1), (2) and (4) above.

IV.23. Loans sanctioned but not to be made available numbered 126 in 1959-60, 144 in 1960-61 and 196 in 1961-62 in respect of all the Corporations. These amounted to 46%, 28% and 27% respectively of the number of applications sanctioned by all the Corporations in each of the above years.

IV.24. Some SFCs e.g., Madhya Pradesh and Rajasthan have, in extreme cases, sanctioned loan applications from small scale units in as little as 1-2 weeks. Generally, the minimum time taken to sanction applications from small units averages about 1-2 months (e.g., Assam, Andhra Pradesh, Jammu & Kashmir, Kerala, Mysore, Uttar Pradesh). The maximum is stated to be 3 months for Orissa, 4½ months for Kerala and Madhya Pradesh, 9 months for Gujarat, 15 months for Andhra Pradesh and 2 years for Assam and Mysore.

IV.25. For others, i.e. larger units, Rajasthan has been able to sanction loans in some cases in only about 8 days. Generally such sanctions seem to take a minimum period of 2-3 months e.g., in Andhra Pradesh, Assam, Kerala, Maharashtra, West Bengal. The maximum ranges from 3 months in Orissa to 27 months in one case in Uttar Pradesh.

IV. 26. The principal reasons advanced by SFCs for delay in sanction, to both small and other units, are—submission of defective schemes, inadequate information and inadequate arrangements for purchase of machinery, inability to submit proper accounts, delay in submission of valuation and their technical reports, legal opinion and banker's reports, etc.

IV.27. In certain SFCs, viz., Andhra Pradesh, Assam, Bihar, Jammu

& Kashmir, Mysore, Orissa, Rajasthan, Uttar Pradesh and West Bengal, sanctions are delayed as they are given only after valuation and legal clearance.

IV.28. In one instance, Mysore SFC disbursed a loan to a small unit within only 2 days of the sanction. Orissa, Kerala, Gujarat and West Bengal have disbursed similar loans in periods of 7, 13, 18 and 21 days respectively. Generally, disbursement takes, on an average, 1-4 months after sanction e.g., in Punjab, Assam, Andhra Pradesh, Jammu & Kashmir and Uttar Pradesh. More time is usually taken for disbursement of loans to medium and large scale units. Though Mysore disbursed such a loan within only 16 days, Orissa within 20 days and Bihar within 26 days, generally it takes 1-3 months. In some instances, Uttar Pradesh and West Bengal SFCs have taken as much as 15 months to disburse a loan. According to Kerala SFC, the delay was longer where loans were sanctioned prior to the establishment of the applicant's title to the property.

IV.29. The major reasons which account for delay in disbursement after sanction are: (1) the borrower's inability to produce clear and marketable title to properties offered as security; (2) his inability to fulfil conditions imposed by the Board of the SFC while according sanction; (3) delay in investigation and legal complications in regard to title deeds and completion of legal formalities; (4) time taken in drafting mortgage deeds; (5) delay by borrowers in furnishing required documents; and (6) delay in importing machinery, construction of buildings, etc.

IV.30. If sanctions are not promptly utilised by applicants, large amouts of SFCs' funds are kept idle in banks, earning low rates of interest. This is necessarily reflected in their income. The source of this difficulty might be lack of knowledge and technical skill on the part of the entrepreneurs to go ahead with their projects. This is also supported by the fairly large number of "applications rejected", "applications withdrawn" and "loans sanctioned but not to be made available" during the three years under review as shown in Table VIII. The percentages of applications "rejected" and "withdrawn" together with the number of "loans sanctioned but not to be made available", to total applications received during the three years were 63, 42 and 54 respectively or an average of 53. Such a high number of infructuous applications entails considerable expenditure of SFCs' resources with no return. Though separate size-wise data regarding rejected and withdrawn applications are not available, they would perhaps be largely from small units.

IV.31. It has been represented that borrowers experience difficulty in securing adequate assistance from SFCs and find their procedures cumbersome. It should be appreciated that most prospective clients of SFCs are men with limited resources who cannot afford the technical services of industrial consultants for preparing their projects. To expect the applicants to fill up complicated forms and answer an elaborate

TABLE VIII

Applications received, rejected, withdrawn, etc. during 1959-60 to 1961-62.

(Amounts in Rs. lakhs)

Year (1)	Applications received (2)		Applications rejected (3)		Applications withdrawn (4)		Loans sanctioned but not to be made available (5)		Total (3+4+5) (6)		Percentage of (6) to (2) (7)	
	No.	Amount	No.	Amount	No.	Amount	No.	Amount	No.	Amount	No.	Amount
1959-60	553	1303.16	81	170.76	141	446.00	126	242.48	348	859.24	62.93	65.94
1960-61	1,035	2143.90	113	267.16	177	401.42	144	232.50	434	901.08	41.93	42.03
1961-62	1,256	2641.23	134	255.95	353	511.72	196	325.43	683	1093.10	54.38	41.39
										Average:	53.08	49.78

questionnaire without assistance is to scare them away. There is often a tendency to reject straightaway loan applications which do not satisfy the various criteria for sanction. The correct approach would be to assist the entrepreneur to so modify his project as to make it acceptable from the point of view of the SFC. In other words, SFCs would have to foster projects, provide guidance and assistance, and steer the different schemes until they can fructify. Further, the legal processes should be made as expeditious as possible and, in the meantime, SFCs might consider granting interim loans in suitable cases as is done by IFC. An essential function of a development bank is fostering new businesses. If SFCs have to fulfil their role, they would have to take more active part in offering technical assistance in the creation and management of new enterprises and reaching out to the entrepreneurial class. As regards proposals rejected for inadequacy of security, the observations of the Group have been furnished later in this Chapter.

IV.32. Applications pending at the end of each of the three years under review showed a steep increase from 241 in 1959-60 to 623 in 1960-61 and 702 in 1961-62. The highest number was in Andhra Pradesh where 155 applications were pending at the end of 1961 and 147 at the end of 1962. The reason given for this was that most of these applications were received during 1960-61 from newly started industrial estates in the State. In Bihar, owing to the shortage of electric power in 1958-59, many applications then received were postponed for future consideration. In Mysore, the arrears are stated to be due to delay by borrowers in furnishing the required information.

(b) Application form

IV.33. A detailed comparative study of the application forms prescribed by the different SFCs as well as MIIC was undertaken by the Group. The forms prescribed by the Corporations are broadly of four different varieties, (*i*) for corporate units, (*ii*) for units other than corporate, (*iii*) for small scale industrial units, and (*iv*) for obtaining information on certain key items before the applicant is to complete a proper application form.

IV.34. The application form for small scale industrial units, as suggested by the Committee set up on the recommendation of the Hyderabad Seminar on Financing of Small Scale Industries, has been adopted almost fully by only two SFCs, viz., of Orissa and Jammu & Kashmir. Punjab and Maharashtra SFCs have included in this form certain other items, information regarding which is to be collected only at the investigation stage according to the Committee. The form suggested by this Committee is simpler than the forms for corporate and other units, (*i*) and (*ii*) above. But it covers all the major items, viz., the constitution and history of the concern; main raw materials required and their sources of supply; annual production and sale; details regarding fixed and working capital; borrowings; purpose of loan; and

security offered. Corporations which have not adopted this form may consider doing so.

IV.35. The preliminary form [item (*iv*) above] has been adopted only in Maharashtra for small scale industrial units. It covers the more important items of the form recommended by the Committee. Where the position of the applicant as disclosed by information supplied in this form appears prima facie satisfactory and acceptable, the applicant concern is then asked to fill the more detailed final form.

IV.36. In addition to the information which Corporations obtain through their application forms and discussions with the applicants, most Corporations have prescribed pre-sanction inspection forms on the lines recommended by Reserve Bank in 1960. Only Punjab SFC has made certain subsequent changes in the form suggested by the Bank, by deleting a few items and introducing certain others. Maharashtra SFC has no specific form for this, but the Inspecting Officer is expected to report on the lines of instructions given to him.

IV.37. The application forms which have been devised are sufficiently comprehensive. They compare favourably with the forms received from some foreign development banks. There may be a few items, however, with regard to which the practice of foreign banks may be of significance to us. Thus, the Pakistan Industrial Credit and Investment Corporation has prescribed two different preliminary application forms —for new industrial units and for existing units requiring finance for extension, balancing and/or modernisation. The two forms are largely similar, but the latter includes additional items seeking information regarding capacity, cost of production, etc. of existing units. Applicants are also expected to give information regarding affiliations of the unit with other groups, if any; experience and background of those in charge of the commercial and technical management of the factory; export potential for and past three years' imports of products to be manufactured; and sales organisation. The Industrial and Mining Development Bank of Iran desires applicants to give information on, inter alia, the following points: position regarding contracts for construction of buildings and/or purchase of machinery; present and projected unit sale price of products of applicants and competitors too; if any market survey has been conducted; and financial summary and financial schedule (cash flow statement) in specified forms.

(*c*) *Security*

IV.38. Sec. 25(2) of the Act requires all accommodation given by SFCs—either as guarantees of loans and deferred payments or granting of loans and advances or subscribing to debentures of an industrial concern, to be "sufficiently secured" by "a pledge, mortgage, hypothecation or assignment of Government or other securities, stock, shares or secured debentures, bullion, movable or immovable property or other tangible assets in the manner prescribed by Regulations" or requires

them to be "guaranteed as to repayment of the principal and payment of interest by the State Government, a scheduled bank or a State co-operative bank."

IV.39. Generally, a registered mortgage of fixed assets, viz., land, buildings, plant and machinery, etc. is accepted as security. Non-industrial assets too are accepted, but as supplemental or additional. Usually the SFCs' General Regulations, apart from stipulating that no loans shall be granted/guaranteed unless sufficiently secured, or guaranteed as mentioned above, also prescribe: (*a*) that for accommodation given under Sec. 25(2), instruments evidencing the security shall be in the prescribed form, no material alteration being made in it without the approval of the Executive Committee/Board; (*b*) that the margins to be retained in the valuation of assets offered as security shall be as considered reasonable by the Executive Committee/Board; (*c*) that the earning capacity and prospects of the concern, the efficiency of its management, etc. must be considered in determining the margin; and, (*d*) that instruments evidencing security must stipulate that if the value of assets pledged, etc. falls, the borrower may be required to furnish additional security as determined by the Executive Committee.

IV.40. Although the General Regulations or the statute do not specifically provide for taking personal guarantee, it is generally taken from directors, managing agents, partners, etc. of loanee concerns as a matter of business prudence. This question was considered at the Seventh SFCs' Conference in the context of liberalisation of policies and procedures; it was recommended that SFCs might waive this condition for well-established concerns with good management and past performance. It is not known if this is being done. Some SFCs also retain a charge on liquid assets e.g., stock-in-trade, book debts, stores, etc. At the Ninth SFCs' Conference, State Bank representatives stated that such a charge makes it difficult for banks to grant working capital loans, and long term loans should be secured with only fixed assets. It was explained at the Conference that SFCs did not normally take liquid assets as security, and in cases where they did so, they would have no objection to release them if borrowers so desired. We recommend that mortgage deeds obtained by SFCs may, as far as possible, provide that their charge over liquid assets would rank after the charge of commercial/co-operative banks providing working capital loans.

IV.41. Generally, SFCs grant loans up to 50% of the value of assets accepted as security. Some have relaxed this, especially for loans to small units: (*a*) Andhra Pradesh—margin has been reduced to 25% on new machinery and 40% on buildings owned by units in industrial estates; (*b*) Bihar and Punjab—40% in respect of sound and feasible schemes; (*c*) Gujarat—relaxed upto 35%; (*d*) Maharashtra—25% in deserving cases; and (*e*) Madhya Pradesh and Mysore—25% if the loan is eligible for guarantee under the Credit Guarantee Scheme. Madhya Pradesh has also brought down the margin for other loans from 50% to 40%.

IV.42. For loans to small units out of Government funds under agency arrangements, the margin is generally 25% as provided in the Rules framed under the State Aid to Industries Acts in some States e.g., Maharashtra, Gujarat, Mysore and Rajasthan.

IV.43. Some further relaxations have been suggested by Chambers of Commerce, Associations, etc. in regard to security, viz.: (*i*) In view of import restrictions, second-hand machinery should also be accepted as security. Although no data are available, it seems that SFCs do sometimes accept such machinery, particularly for small units. However, the point is valid ; SFCs may examine for further relaxations. (*ii*) Hypothecation of machinery spares and machinery stores along with the main plant should not be insisted upon. It may not be advisable for the Corporations to agree to this suggestion particularly in view of the present import restrictions, since the disposal of spares and stores by the borrower may render the machinery idle for indefinite periods. However, they may consider making exceptions in deserving cases. (*iii*) Personal guarantees should not be insisted upon, if adequate security is available. But SFCs do not universally insist upon such guarantees, and even banks take them. For concerns with good past record, particularly joint-stock companies, this requirement may, no doubt, be waived. In any case, such guarantees are necessary for loans to proprietary and partnership concerns.

(*d*) *Valuation of assets*

IV.44. Apart from the margin, the quantum of assistance also depends on the valuation of assets. A relaxation in the margin may be neutralised if assets are valued very conservatively. Broadly, there are three methods of valuation, viz., (*i*) book value, (*ii*) current market value as estimated by experts and (*iii*) replacement value less depreciation for the number of years the asset has been used. The practice of different SFCs especially for plant and machinery, is as follows: (*a*) Andhra Pradesh—book value, engineers' valuation or market value, whichever is lower; (*b*) Assam—normally market value; (*c*) Bihar—original cost less depreciation; (*d*) Gujarat—for new machinery, cost of components and manufacturing cost of machinery; existing machines are valued at book value minus depreciation for number of years in use; (*e*) Jammu & Kashmir—market value less depreciation; (*f*) Kerala—final valuation on the basis of original or purchase price less depreciation; (*g*) Madhya Pradesh—for new machines, cost (including erection charges) as per account books and for old ones, market value after taking into account the number of years used; (*h*) Madras—new: invoice value (including all charges for erection, etc.); used: replacement cost less depreciation; (*i*) Maharashtra—new machinery is valued on the basis of written down value in the audited balance sheets; in case of inadequate depreciation, it is worked out at the rate of 10% per annum; valuation of second-hand machinery is done on the basis of expert opinion; (*j*) Mysore—

based on age, working condition, etc.; (*k*) Orissa—on the basis of cost as shown in suppliers' invoices less depreciation; (*l*) Punjab—depreciated or assessed value, whichever is less; (*m*) Rajasthan—old plant and machinery are valued after allowing depreciation at the Income Tax Department rates; for new machinery, cost price as per suppliers' invoice is taken; for non-standard or fabricated machinery, assessors' valuation is taken; (*n*) Uttar Pradesh—invoice value plus freight, duties, insurance, transport and erection charges in respect of new machinery; replacement value less depreciation in case of old, after taking into consideration condition of the machinery, maintenance and upkeep, etc.

IV.45. This question has been discussed at some of the SFCs' Conferences. The First Conference, in discussing the merits of different methods, suggested that the adoption of "book value" might not be appropriate where a concern had written down the value of an asset to a nominal figure though its market value might be much higher. It might also be contended that "market value" at a particular time may not afford a proper basis to adopt for term loans, repayable over many years. It was generally agreed that a combination of one or more of these bases of valuation was desirable to safeguard the interests of SFCs and also the borrowers. The matter came up again at the Third Conference. The Seventh Conference discussed if, for urban land and buildings, market value should be considered, and if the capital value of assets should also include items like installation charges, technical know-how fees and interest on borrowed funds during construction. It was decided not to lay down any rigid policy.

IV.46. A question which often arises is whether the practice of taking fixed assets at depreciated book value does not unduly undervalue them in relation to what they may fetch in the unlikely event of a foreclosure of the loan, and the disposal of the assets as part of a going concern. Plant and machinery are generally depreciated annually (particularly by limited companies) at rates allowed by the Income Tax Department, which in most cases is about 10% or more. After some years, the book value of a machine may be very nominal though its market value may yet be appreciable if well maintained; if such assets are taken at the depreciated book value, the security offered may not be adequate for the credit required by the borrower. It may, therefore, be necessary to consider the market value of the security also in deserving cases.

IV.47. In States like Assam, Mysore, Punjab, Madras and Uttar Pradesh, there is no difficulty regarding the clarity of title to land offered as security. In others, viz., Andhra Pradesh, Rajasthan and Jammu & Kashmir, difficulty arises mainly in areas where agricultural lands can be alienated only with sanction from revenue authority. In Bihar, the difficulty is stated to be only for lease-hold or mining lands; in the former case, borrowers must get the rights of sale and transfer assigned in their favour, and in the latter, to get Government's permission to mortgage mining lands to the SFC. In Madhya Pradesh and Gujarat, title deeds

are not easily available in areas of old princely States and the diversion of land to non-agricultural uses is a lengthy legal process. In Orissa, difficulty arises for land situated in areas which have yet to be surveyed and settled. In some areas, interest in land cannot be transferred because of special local systems of land tenure. For agricultural land, the Land Reforms Act there, it is stated, may also prejudice the interests of SFCs. State Government have taken up survey and settlement operations in areas where SFC experiences difficulties and are examining how far the Land Reforms Act is prejudicial to the Corporation's interests. In Kerala, recent land legislation, it is stated, has upset most titles to land.

IV.48. With a view to removing difficulties in establishing clarity of title to land, it has been suggested by one SFC that suitable legislation may be enacted to declare a title valid if it is clear for 10 to 15 years. This suggestion cannot be accepted as fairly long periods of limitation are prescribed for enforcement of claims in respect of immovable property. A mortgage created about twenty years earlier may still be subsisting, if it has been kept alive by the mortgagor. Or a Government may have some interest in the property, in which case it has sixty years within which to enforce its right. This suggestion involves cutting down substantially the periods of limitation now allowed for enforcing rights and is, therefore, extremely unlikely to be accepted. Except in the cases mentioned above, there does not appear to be much difficulty elsewhere about the clarity of title to land. Where it is not quite clear, State Governments may take suitable steps to remove the difficulties.

IV.49. The Sixth SFCs' Conference (1959) requested Reserve Bank to examine the difficulties of Bombay SFC in assisting units situated on rented premises or premises not assignable to it, due to the provisions of the tenancy law. The Bank advised as follows--The General Regulations of SFCs require that, in granting accommodation reasonable margins are to be maintained, taking into account, inter alia, the managerial competence, earning capacity and prospects of the concern, etc. If reasonable margins are maintained to the satisfaction of SFCs, loans given on the security of assets mortgaged by such concerns can be deemed to be "sufficiently secured" within the meaning of Sec. 25(2). Further, the machinery installed in the premises of the type under consideration could, *if it is immovable property,* be mortgaged to the Corporation by registered deed, thereby creating an effective security in its favour. It could not be said, therefore, that loans to such concerns granted on the above basis were insufficiently secured.

IV.50. But advances to such concerns presented some difficulties; in case of default, the SFC would not be able to exercise all its rights under the SFCs Act, especially, to have possession of the premises. It was felt that these legal impediments need not come in the way if plant and machinery offered as security belonged to the *"movable"* category, provided the earning capacity, management, etc. of the concerns were

good. The Bank noted that there was no difficulty in accommodating such concerns and felt that the question of requesting the State Government to review the tenancy laws in this connection would arise only if there were many requests from such concerns for advances which the SFC was unable to meet because of the above considerations. The Maharashtra Government took note of these difficulties. To facilitate the making of advances to units on rented premises, in March, 1961, Government issued a notification permitting the transfer or assignment of any lease-hold premises (irrespective of the period of the lease) to the SFC or the State Government as part of or incidental to a mortgage of any lease-hold premises, including the factory thereat, by an industrial concern eligible for assistance under the SFCs Act or the State Aid to Industries Rules.

(*e*) *Appraisal*

IV.51. On the question of appraisal of term loan applications, detailed recommendations have been formulated by the "Working Group on Appraisal of Applications for Term Loans" set up by Reserve Bank. It will be of advantage if the staff of SFCs handling loan proposals familiarise themselves with the essential requirements of appraisal of term credit. The present methods of appraisal are often very far from even such preliminary recommendations as the Group has made, having Indian conditions in mind. Instead of going into details which have been competently discussed by the above Group, the observations here will be confined to some of the critical factors for appraising a proposal for term loan. It may be emphasised that for SFCs to combine banking and developmental criteria will be the hallmark of this operation.

IV.52. By way of an introduction we may indicate that, unlike short term working capital loans which require only short term forecasts, quick turnover and easy liquidity, inherently greater risks are attached to term loans which must be dealt with by special skills. It is much more difficult to estimate a borrower's creditworthiness 10 or 12 years ahead than over a short period of 6 or 12 months. The factors relevant to creditworthiness are substantially different over the longer period. The capacity and experience required in the appraising personnel for assessing them are of a different order.

IV.53. Security—Many prospective borrowers and even loan officers believe that if sufficient security is offered, the credit institution ought to make the loan without question. It may be emphasised that security does not improve the credit although it reduces the risk, and in most cases the need for security reflects some weakness in the credit. Security makes the lender a preferred creditor but does not necessarily make the loan a wise one. Basically, a long term lender wants to get his money back from the normal operation of business, after it has served the purpose for which it was borrowed, but he does not want to have to take

over the security and liquidate the business. Apart from this, unlike self-liquidating commercial loans against the security of commodities, stocks, shares, bills receivable, etc., term loans to industries are granted mainly against the security of fixed assets not intended for resale but to be used for production ; therefore, the repayment of a loan should come not from the sale proceeds of the assets forming security but from the earnings of the concern. Further, fixed assets are difficult to dispose of even in good times ; their forced sale might fetch meagre value. Secondly, term loans are not repayable on demand but according to a schedule of repayment extending over a number of years and thus the ability of the lender to convert the assets into cash is restricted. Thirdly, the lender has less control over the security as it all along remains in the possession and use of the borrower, and the lender does not have the same freedom to deal with it as in the case of an effective pledge of movables. Thus, unlike short term commercial loans, in the case of a term loan the lender cannot remain satisfied with the secured nature of the advance and current prices of the items of security. He has to closely examine the feasibility of the project while sanctioning the loan and to watch the prosperity of the industry and concern himself with the activities of the borrower throughout the currency of the loan. This does not mean that no security should be obtained. It is usual to obtain as security a mortgage of the physical assets of an enterprise while lending on term basis. Though it is of secondary importance, it has its uses. The power of foreclosure available under the mortgage deed may serve to reinforce the lender's influence over the policies of an enterprise in difficulties. If that influence can be exercised sufficiently early, difficulties may be anticipated and the profitability of the enterprise, the true security for the loan, may be protected. However, the security cover for the loans should not be regarded as a substitute for proper financial assessment. In fact, the security requirements could be relaxed or waived in deserving cases having regard to other relevant factors.

IV.54. More concern with earning prospects and less with security will open the way for SFCs to helping deserving enterprises particularly new ones which may not be able to provide conventional security or guarantee but have an acceptable scheme and are managed by technically qualified and competent persons. Obtaining maximum security, as is generally the present practice, reduces the range of flexibility of SFCs and, subconsciously if not consciously, causes a stress upon caution in loan policies, which impedes progress. The emphasis on security also presumably accounts for the difficulty encountered by persons who are new to industry or who are not well known, in meeting their financial needs and most of them are driven to non-institutional lenders.

IV.55. Unless the borrowing company has a very strong balance sheet—this is unlikely in the case of smaller industries with which SFCs mostly deal—the only valid test of ability to repay at the end of a long term is appraisal of long-range earning power. Over a period of years,

only the continuation of satisfactory earnings will maintain the balance sheet position, and poor earnings can cut away assets rapidly. The ability to appraise future earning power is needed not only for sound evaluation of term loans. It can also be fashioned into an effective competitive weapon. Any loan officer can make a 7-year loan to first class established houses with a high credit standing. But contrast this with the case of a little-known small enterprise which wants to borrow Rs. 2/3 lakhs for 7 years. The lending agency which employs the earning appraisal method in processing term loans is not only in a position to offer such a loan more soundly but also more competitively.

IV.56. The necessity for assessment of the financial soundness of the venture assumes greater importance in the case of small scale industries. It is recognised that small scale units do not often maintain proper accounts; where they maintain them, they are sometimes unwilling to disclose them. Often, the books are not kept up-to-date. The balance sheets and profit and loss accounts are in many cases out of date and, therefore, do not offer much guidance to the present condition of the business. But whatever the difficulty in their preparation and presentation, the importance of a study of past performance, present financial position, and future prospects cannot be ignored. The maintenance of proper and up-to-date accounts is vital not only from the point of view of a lender but also of the borrower himself who should know his precise position to plan future programmes of production, expansion, etc. A borrower who carries on his business without knowing where he stands is obviously a bad risk. On the other hand, when he wants others to rely on his credit without himself first establishing it, he is obviously not playing fair and has to be dealt with cautiously. Thus, what is required is a drive for mutual understanding and persuasive effort on the part of the lender which may sometimes mean offering a little guidance to the borrower to maintain his books in the acceptable form.

IV.57. Project analysis—An essential requirement for appraisal of a term loan is the scheme in respect of which the loan is sought. It may either be to establish a new unit or for the expansion, modernisation, etc. of an existing one. The scheme broadly indicates the various requirements of fixed and working capital and how the expenditure thereon is to be met, the various sources from which the funds are proposed to be raised, the components of raw materials and their supply position, the prospects of the industry and the economics of working, showing the expected profits and availability of cash for repayment of the loan. All this requires a careful planning and budgeting and as such it is necessary that the scheme should be drawn up by, or in consultation with, persons sufficiently experienced in this line. Smaller units do not often prepare such schemes but estimate their requirements in a haphazard manner. The result is that sooner or later snags become apparent, and either the project has to be scrapped half-way or, if completed, its working becomes uneconomic and unremunerative. A purposeful exami-

nation of the scheme in its technical, economic and financial aspects, however limited in scope for investigation in the circumstances of a particular case, has nevertheless to be made.

IV.58. Debt-equity ratio—Normally, the main source of financing fixed capital requirements of an industrial unit is equity capital and it is essential to require an entrepreneur to put up substantial matching funds. Ordinarily, a debt-equity ratio of 1 : 1 is considered satisfactory though in deserving cases some relaxation should be allowed having regard to other favourable factors. It is important to ensure that a unit's borrowings are not disproportionately large as compared to its equity base, as the weight of such borrowings may be too heavy for a unit to bear and affect the ultimate recovery of the term loan out of future profits. Besides, reasonable entrepreneurial stake is an essential requirement. A lender must be on his guard against having too large an interest in the success of a business. Sufficient proprietary stake ensures a more cautious and purposeful handling of the affairs by the management. Further, adequate equity imparts greater flexibility to the operations of the units and improves their shock-absorbing capacity or provides a cushion against adverse circumstances which cannot be anticipated when granting the loan. Market demand for the goods manufactured by the unit might dry up or there might be delays in the recovery of sale proceeds.

IV.59. Loan supervision and follow-up—It is essential for a long term lending institution not only to control the rate at which funds are withdrawn but also to scrutinise the execution and operation of the project which is being financed. The object of such supervision is to keep the institution informed of progress, and to provide opportunity for advice in anticipation of difficulties and for assistance if trouble ultimately arises. In the case of new enterprises, or during the initial period of the loan, reports should be called for more frequently than in the case of established enterprises with a satisfactory history of successful operation. It is also considered advisable to conduct periodical inspections more frequently in the case of risky or new enterprises or where difficulties have arisen.

IV.60. Enterprises in difficulty—Notwithstanding careful supervision, some enterprises are bound to fall into difficulties. Sometimes it suffices to reschedule principal and interest payments. Sometimes the enterprise is persuaded to engage competent technicians who can diagnose and cure the trouble. It may also be necessary for the lending institution to foreclose and dispose of the assets in order to save its investment. The decision whether to foreclose or to try to keep an enterprise going is, of course, influenced by the saleability of the assets. Where the assets are difficult to dispose of (perhaps because of their location or special design) it might be necessary to make efforts to rehabilitate the enterprise by putting in new management, working out a financial reorganisation, assisting in devising new marketing arrangements, etc.

There will be less difficulty in the case of a standard enterprise which has failed, as purchasers are readily attracted to take advantage of trained labour and the possibility of acquiring assets at a considerable saving.

IV.61. A SFC is expected to evaluate a credit risk by taking into account the management, and economic and financial risks. Each of these should be weighed in relation to the others and should be considered in connection with the size of the commitment, the length of time it is to run and the economic desirability of the transaction. There is no one easy road to the evaluation of credit risk as circumstances alter the approach in each case. It should also be remembered that a safe loan is a loan that, to the extent determinable, is free from ultimate loss. A sound loan is a safe loan that can be repaid within its maturity terms without hardship or stress on the borrower. It is not enough for a loan to be safe; it must also be sound. A borrower must not only have adequate financial strength or adequate security, he must also have adequate repayment ability. However strong the financial strength or however good the security, this question should always be asked "How is the borrower going to pay it back?"

IV.62. There are certain reasons which invest the question of appraisal by SFCs with some importance.

(*a*) Presumably to keep down administrative expenses and, thereby, losses and drawing of subvention from the States, almost all SFCs have avoided recruiting the minimum technical personnel necessary for appraisal as well as follow-up and supervision during the currency of the loan. The Working Group on Appraisal has stressed the need for such staff to undertake these functions; it clearly states that each lending institution should have a minimum complement of one team consisting of trained and experienced persons from each of the three fields—engineering, industrial economics and accounting, at a fairly senior level. (This is again discussed in Chapter VI, paragraphs 44 and 45).

(*b*) In the absence of such technical staff, and consequently the reliance on the often disconcertingly long time-consuming process of the local technical officers of the State and Central Governments for scrutiny of loan applications, SFCs have tended to concentrate their advances in the better known, traditional sectors of industry, and to avoid the less known but newer types of activity. This is evident from an analysis of their loans and advances. It has some serious implications. In order to tone up the industrial structure and to gradually pave the way for a greater diversification of exports, the unorthodox sectors of industrial activity are to be consciously encouraged by SFCs. There is another aspect too. These new kinds of industries generally have a higher growth rate and profitability as compared with the traditional industries. If SFCs recruit the necessary minimum complement of technical staff and conciously align their activities with the trend towards setting up the more modern types of industries, they would be rendering a service to the economy and ensuring larger business for themselves in the future.

(*c*) In the existing set-up, SFCs tend to put excessive emphasis on the security aspect of the propositions placed before them rather than on their economic viability. They seem to associate the repayment of their loans with the sale of the security; but, as indicated earlier, assets offered as security are often difficult to dispose of as they do not ordinarily have a ready and regular market. Their worth, which is estimated on the basis of a "going concern", largely depends on the earning potential of the project as a whole. The methods now followed may conceivably result in eliminating a number of proposals which would stand scrutiny on the basis of prospective profitability.

(*d*) Lastly, when applications are passed through the sieve of a proper appraisal procedure, units which have a higher growth potential and profit earning capacity will be separated from the others and it will pay the Corporations to concentrate their resources on such propositions. These would repay the loans earlier than others and capital formation would generally be quickened.

IV.63. It has been an oft-voiced demand that SFCs should relax their security requirements and criteria. The efforts so far made, generally as also for the small borrowers in particular, are indicated above, and the lines on which further action is to be taken by the States, the Central Government or SFCs to implement agreed decisions have also been indicated e.g., freeing liquid assets from mortgage charge, adopting more realistic and borrower-oriented basis for valuation of securities, removal of difficulties to the title of land in certain areas, etc. As these recommendations are implemented, there should be considerable relief, and SFCs would be able to function more expeditiously.

IV.64. SFCs, on their part, should also consider softening the rigour of the tests they apply for assessing their borrowers. Not that they should abandon all caution, as they are expected to pay their way and earn a reasonable profit. But they should remember that no lending operation can be undertaken without a certain element of risk. And as the sector to which they cater is relatively weak, they should, in their financing decisions, place more emphasis on the prospective profitability of the project to be financed than on security. If they are convinced that the project is economically viable and the borrower satisfies the tests of technical competence and personal integrity, a less rigid attitude on their part will be called for. There will be, of course, certain limits beyond which it is not possible to proceed, since the borrower must have a minimum stake in his concern, and there will always tend to be an aura of uncertainty about the future of a concern, or the realisable value of its assets if the concern has to be wound up, which surrounds even a detailed appraisal report. One way of helping a deserving entrepreneur starting a new business would be to allow some relaxation in the margin requirements, which will enable him to have a larger margin for manoeuvre in the difficult early years of operation. This will also enable him to utilise some portion of the loan to meet his requirements of

working capital, which a commercial bank may not be willing to provide until he has established himself in business.

IV.65. It is also to be noted that SFCs were specifically set up to finance small and medium-sized units which cannot turn elsewhere for the credit they require except at a very high cost. There is increased pressure on the resources of the larger financing agencies like IFC and ICICI, as large borrowers now prefer to go to them rather than to the capital market which is in a bad shape. Commercial banks have no doubt taken some interest in term lending lately, but their capacity is bound to remain limited so long as they do not have surplus funds after meeting the working capital needs of industry. Under the impact of accelerated development plans and the emergency, demands on term lending institutions are expected to grow rapidly in the near future. SFCs' success in facing this challenge will depend on how promptly and adequately they meet the changing needs of a growing economy. If they fail, they will have lost an opportunity to contribute to industrial development and in the process grow into strong institutions. For meeting the credit needs of small scale units, many of which are not good risks, SFCs should make greater use of the Credit Guarantee Scheme for small industries. This scheme has been extended to the whole of the country and would help SFCs to minimise the risk of this business.

IV.66. We must emphasise that the main aim of SFCs should be to see that the units they assist become viable in due course. The capital resources of the country are too scarce to be wasted on inefficient units. SFCs should, therefore, equip themselves fully to undertake post-credit services and should insist that their clients adopt modern productivity techniques. Credit is an important but not the only element for raising the productive capacity and efficiency of smaller industries and a too exclusive emphasis on credit alone is likely to lead to the establishment of units which become a drag on the economy and create more problems than they solve. There is, therefore, a great need for an integrated approach to the development of small industries.

IV.67. It appears that to some extent the rigid attitude displayed by SFCs as revealed by their past operations has been the direct result of the provision of section 25(2) of the State Financial Corporations Act, which, as indicated earlier, provides for loans, guarantees, etc. to be made against *sufficient* security or guarantee. This statutory provision has led SFCs to obtain maximum security irrespective of the prospective profitability of the applicant concerns or the competence of their management, thus reducing their (SFCs') range of flexibility and forcing them to exercise excessive caution which has impeded their progress. We suggest that this statutory provision should be amended by substituting the existing section 25(2) by the following:

> "Section 25(2)—In determining whether or not accommodation shall be provided under clauses (*a*), (*b*) and (*g*) of sub-section (1), regard shall be had primarily to the prospects of the operations of

the industrial concern and the accommodation shall be secured by tangible security or guarantee of the State Government, a scheduled bank, a State co-operative bank or others to the extent which may be considered by the Board to afford a reasonable protection."

IV.68. To relax the present statutory provision does not mean that SFCs would lend without adequately protecting their interests. What it does mean is that, in deserving cases, the directors will have the necessary manoeuverability to accommodate new projects and the new class of entrepreneurs struggling to find a place in the industrial map of the country; also small scale industries which are often unable to provide conventional security but have an acceptable scheme and are managed by competent persons. Development banking, we have already stated, invariably means taking risks; where the statute ties the institution down, progress is bound to be slow. Provisions similar to those proposed above find place in the constitutions of the Industrial Development Bank of Canada and Commonwealth Development Bank of Australia. If this step is taken, the way will then be paved for the conversion of these SFCs into development banks proper.

IV.69. In addition to the grant of loans and advances to industrial concerns, the Act provides for certain other types of business which SFCs can conduct with industrial concerns to assist them. Thus, under Sec. 25(1)(*a*) they can guarantee loans raised by industrial concerns which are floated in the public market or obtained from scheduled and State co-operative banks. Under Sec. 25(1)(*b*), they may guarantee deferred payments due from a concern in connection with its purchase of capital goods within India, and under Sec. 25(1)(*g*), they are permitted to subscribe to the debentures of an industrial concern. (The various considerations bearing on these sectors of the business of SFCs are taken up later).

(*f*) *Lending rates*

IV.70. In the early years, the few SFCs then functioning charged interest on their loans at 6% to 6½% per annum, net, with a loading of one-half of one per cent for late payment. A few SFCs like those of Punjab and Assam had two different rates depending on the size of the loans—in 1954 and 1955, the net rates in Punjab were 6½% for loans below Rs. 2 lakhs and 6% for larger loans; during 1956-58, Assam charged 7% net for loans below Rs. 1 lakh and 6% net for larger loans. Orissa introduced a similar differentiation, but as late as in 1962 and only for a little over 6 months—to foster small loans, those below Rs. 2 lakhs paid 6% net, others 6½% net.

IV.71. Punjab SFC furnishes the major instance of linking the lending rate with the Bank Rate. From 1st May, 1957, by which time the differentiation of rates as between different sizes of loans had been given up, upto 6th February, 1958, the lending rate was 2½% above the Bank Rate, subject to a minimum of 6½%. On 16th May, 1957, the Bank Rate was raised from 3½% to 4%. In February, 1958, therefore, the lending

rate became 3% above the Bank Rate, subject to a minimum of 7%. After the Bank Rate was raised to 4½%, the rate was fixed at 7½% net. Uttar Pradesh SFC has such a link since 1962; 3% above Bank Rate, subject to a minimum of 7%, now raised to 7½%, with a rebate of one-half of one per cent for timely payment.

IV.72. Between July, 1962 and January, 1963, a considerable measure of uniformity has been reached. The usual rate for all SFCs now is 7% net, with a loading of one-half of one per cent for late payment. The exceptions are:—Punjab—7½% with no rebate and Jammu & Kashmir—6½% net with loading for late payment. Allowing for the cost of funds raised by most SFCs at about 5%, they are left with a margin of 2% out of which they must meet administrative expenses and guaranteed dividends, and slowly build up reserves, after payment of taxes, to cover risks of default. The lending rates of IFC and ICICI are 7% net, and 6½% to 7% net respectively, which are more or less the same as those of SFCs. Having regard to the fact that SFCs cater to the needs of smaller industrial units which have higher mortality rate than the larger units generally financed by IFC and ICICI, and that the cost of administration per enterprise financed is the same irrespective of its size or the size of the loan, 2% return is hardly justified. No wonder that this, aggravated by the provision of guaranteed dividends, has resulted in meagre reserves and growing subvention liability to State Governments. It is significant that as compared with other SFCs, Punjab SFC, which now has the lowest subvention liability, charges one-half of one per cent higher interest on its loans and pays a like amount less on its shares. Along with West Bengal SFC, it ceased to draw subvention after 1960-61.

IV.73. It may be emphasised that SFCs were meant to provide funds which otherwise were not available—not to subsidise industry by financing them at lower than the economic rate. Even such margins as SFCs now have are likely to be further reduced. Their effective borrowing rate by means of bonds, including all expenses, is already above 5%, and it is apparent that this rate will now go up further if institutional investors who make up the bulk of the investors for these bonds are to be attracted.

IV.74. Considering all these factors, the present lending rates require to be adjusted to allow the Corporations to have a margin of at least 2½%. It may be argued that industrial units may not be able to bear the higher rate. But the incidence of interest on the cost of production is small and the rate of profit in a controlled economy is high. Industrialists are prepared to pay even 9% to 9½% on preference shares and a slightly higher rate on their borrowings is not likely to affect them adversely.

IV.75. Apart from this, consideration should also be given if, instead of a standard rate for all loans, an appropriate rate structure may not be evolved, the rates varying with the risk-rating of different propo-

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sitions, their size, period, etc. A uniform rate restricts SFCs financing only the best long term risks, whereas higher rates for higher risk might encourage them to extend financial assistance to more marginal firms.

(g) Charges other than interest

IV.76. Small borrowers often maintain that SFCs levy disproportionate charges for such items as application fees, valuation, legal examination of documents, etc. To examine this matter, the Working Group requested the Corporations to furnish the schedules of such charges. As the incidence of these charges would not be evident from such schedules alone, they were also requested to give the actual quantum of such charges—under each separate category—borne by about half-a-dozen each of their small and other borrowers, and the loans sanctioned to them.

IV.77. The charges were broadly grouped under nine heads—for application, technical appraisal, valuation, legal scrutiny, inspection, commitment, stamp duty, registration charges and others. Apart from stamp duty and registration charges, governed by State Government rules, the first thing that strikes one about these charges is the variety of bases adopted for them, and the consequent differences in incidence. Thus—

(*i*) Application fees: Eight SFCs make no charge. Two others charge only nominal amounts. The rest four SFCs and MIIC charge on the basis of the amount applied for, but in very different ways. MIIC and Mysore levy consolidated fees for application, technical advisers, valuation and legal scrutiny. (*ii*) Technical advisers: In West Bengal, Kerala and Bihar, there is no schedule of charges; borrowers pay ad hoc amounts, if necessary. In Uttar Pradesh, they are charged travelling allowance for SFC and State Government employees at prescribed rates; for others, actual expenses incurred are recovered. Gujarat makes no such levy at present. (*iii*) Valuation: In addition to fees of technical advisers, Uttar Pradesh SFC recovers travelling allowance charges or actual expenses, as the case may be, for valuation. In West Bengal, Kerala and Bihar ad hoc amounts are charged, being usually 25 nP.% in Bihar. Elsewhere, there are varying schedules, depending upon the assessed value of property and its nature. (*iv*) Legal fees: Regular rates are laid down by only a few Corporations. (*v*) Inspection charges: Schedules have been prescribed only in Rajasthan and Punjab. Bihar has detailed rules for pre-sanction inspection and periodical post-disbursement inspection. Elsewhere, either no charges are levied or travelling expenses are recovered. (*vi*) Commitment charges: Only six Corporations have reported these charges, on widely varying bases and rates. (*vii*) Stamp duty and Registration charges: Rates vary much from one State to another. (*viii*) Other charges: The only other charge mentioned is the guarantee fee of 25 nP.% under the Credit Guarantee Scheme.

IV.78. Ten SFCs and MIIC sent data on the charges borne by 65

small borrowers and 70 large borrowers to whom loans aggregating Rs. 75.47 lakhs and Rs. 559.97 lakhs respectively had been sanctioned. In order to compare the charges borne by the small and large borrowers, the aggregate charges borne by them separately under each head was expressed on a per Rs. 1 lakh of sanction basis. No quantitative precision can attach to the comparison between charges borne by small and large borrowers for any Corporation or among small and large borrowers separately between Corporations as, apart from the question of accuracy of these data, comparability is also affected by another factor, viz., that the companies selected may not represent the groups adequately in the sense especially of the extent of the need for technical advice, valuation, legal scrutiny, inspection, etc. (since charges are on amounts applied for, and often smaller amounts are sanctioned, the varying extent of cuts while sanctioning also affecting comparability). Where some companies in any group have not paid a particular charge, the average per Rs. 1 lakh of sanction has been calculated for the sanctions to the entire group as also for what is sanctioned to only those concerns which have borne this charge. These latter averages are shown within brackets below. For each type of charge, the first figure represents the average for small concerns and the next one for larger concerns:

(*i*) Application fee; Kerala—971 and 898; Madras—725 and 113; Mysore—1376 and 632. (*ii*) Technical adviser; Kerala—542 and 209; (*iii*) Valuation: Assam—119 and 84; Madhya Pradesh—317 and 130; Madras—174 and 34; Maharashtra—277 (554) and 113; Punjab—282 and 58; Rajasthan—122 (127) and 67. (*iv*) Legal scrutiny; Bihar—282 and 30; Kerala—97 and 70; Madhya Pradesh—134 and 56; Madras—130 and 14; Maharashtra—1257 and 382; Punjab—134 and 27; Rajasthan—Nil and 63. (123); Uttar Pradesh—100 and 65; West Bengal—694 and 481.

IV.79. The outstanding feature of these charges is their uniformly heavier incidence on small borrowers. This is primarily due to the adoption of the slab system, with a minimum charge payable by all borrowers upto a specified amount applied for, with decreasing proportionate charges in the higher slabs. Even if these figures do not exactly reflect the absolute magnitude of those charges, the relative incidence on small and large borrowers is very unlikely to be reversed with more refined sampling methods.

IV.80. It may be contended that for many of these services, the Corporations incur certain overhead charges; as these do not vary directly with the size of assistance, the charges cannot be uniform for all borrowers. There is perhaps some force in this argument. But since for the most outstanding element of cost to the borrowers, viz., interest, no discrimination is made either with regard to size, risk, or period, of loans to them, to introduce discrimination, however small in magnitude, in favour of the large in the levy of these other charges does not appear justifiable.

IV.81. This is as regards the relative incidence on small and large borrowers for any one Corporation. The figures also indicate fairly substantial variations among the different Corporations. It may be worthwhile attempting to reduce these differences and bring the rates to a more comparable basis. Taking all the charges together, their average incidence on small and other borrowers are 2.51 and 1.99 per cent respectively for all the eleven Corporations which have supplied illustrative cases. In the case of the small borrowers, the incidence is more than these figures indicate as most loans to them are for much smaller periods than those to other borrowers.

IV.82. Registration charges and stamp duty levied by the State Governments are generally seen to bear almost equally on all borrowers except in West Bengal, Maharashtra, Bihar and Punjab where the incidence seems heavier on small loans.

IV.83. In a note submitted to the Hyderabad Seminar (1959) Shri B. N. Mehta, Legal Adviser, Reserve Bank of India, had suggested that as far as loans to small units were concerned,

(*i*) State Governments might, under Section 9 of the Indian Stamp Act, or any corresponding law in force, remit or reduce stamp duty payable on mortgage deeds; and

(*ii*) they might be enabled to remit or reduce registration charges.

IV.84. Later, directed by the Small Scale Industries Board, the matter was taken up by the Committee on Credit Facilities, which set up a Sub-Committee to examine the pattern of stamp duty, registration fees and other charges levied on loans to small scale units, and make suitable recommendations. These recommendations, endorsed by the main Committee, were as follows:

The following documents should be supplied free of cost by the authorities concerned—(*i*) valuation certificate in respect of land and buildings, (*ii*) non-encumbrance and title to property certificates in respect of land and buildings, (*iii*) drafts of mortgage deeds and surety bonds and/or guarantee bonds. It also suggested the maximum rates of stamp duty on (*a*) personal bonds, (*b*) surety or guarantee bonds and (*c*) on mortgage deeds. For mortgage deeds, it had suggested complete exemption for loans upto Rs. 5,000. The Sub-Committee also suggested the exemption of personal bonds, surety bonds and/or guarantee bonds from registration fees and certain maximum registration fees on mortgage deeds. It had also suggested that other incidental charges for documents, copying charges, legal fees, etc. should not be levied at rates higher than the following:—(*a*) on personal bonds, surety bonds and/or guarantee bonds—nil and (*b*) on mortgage deeds, at Rs. 10.15 nP.

IV.85. The Small Scale Industries Board considered these recommendations in February, 1961, and decided that instead of the uniform and liberal scales of stamp duty, etc. suggested by the Sub-Committee, as the existing rates differed widely in the various States, it would be more desirable to recommend that for loans to small units, the States charge

only 50% of their normal rates. It also endorsed the recommendation for the free supply of (*a*) valuation and non-encumbrance certificates in respect of land and buildings and (*b*) draft of mortgage deeds and surety bonds and/or guarantee bonds. The Working Group on the Appraisal of Applications for Term Loans also recommended that pending an amendment of the statute, the States may consider allowing reduction in the stamp duty and registration charges on loan documents.

IV.86. These recommendations were sent by Central Government to the States for implementation. The present position seems to be: Valuation certificates in respect of land and buildings and draft mortgage deed are supplied free of cost in Assam, Delhi, Himachal Pradesh, Jammu & Kashmir, Orissa and Rajasthan. In Delhi, Himachal Pradesh, Orissa and Rajasthan, non-encumbrance certificates in respect of land and buildings and surety and guarantee bonds too are supplied gratis. In Himachal Pradesh, Jammu & Kashmir and Rajasthan, small units assisted under the State Aid to Industries Act pay no or reduced stamp duty and registration fees on loan documents. In Maharashtra, upto November, 1961, small units borrowing upto Rs. 5,000 under the State Aid to Industries Rules were exempted from stamp duty chargeable under the Bombay Stamp Act, 1958. On 1st December, 1961, the Maharashtra State Aid to Industries Act, 1960 and Rules, 1961 came into force but as Government have not yet issued a notification exempting small loans upto Rs. 5,000 from stamp duty as before, such loans now pay stamp duty from 1st December, 1961. Registration charges have been payable all through. The Kerala Government hold that it is not advisable to adopt measures which decrease Government revenue in a period of emergency, and that loans being issued to small units should be adequate assistance for them. Non-encumbrance certificates are supplied free. Efforts should be made by all State Governments to implement the recommendations of the Small Scale Industries Board at an early date.

Chapter V

DEPLOYMENT OF RESOURCES (CONTINUED)— LOANS AND ADVANCES

Breakdown of loans by constitution of industrial concern

V.1. While Sec. 2(*c*) of the IFC Act, 1948, interpreted an "industrial concern" as any public limited company or co-operative society engaged or to be engaged in certain specific types of business, there is no such limitation in the SFCs Act. We show below the breakdown of the outstanding loans of SFCs as on 31st March, 1962 (such data are not available for MIIC) according to the constitution of borrowing concerns.

Percentage breakdown of SFC loans outstanding—constitutionwise— as on 31st March, 1962.

Classification according to constitution	Amount (Rs. lakhs)	%
1. Proprietary	228.56	12.3
2. Partnership	499.25	26.8
3 Hindu Undivided Family	44.19	2.4
4. Co-operative	23.17	1.3
5. Private Limited Company	567.77	30.4
6. Public Limited Company	498.30	26.7
7. Co-ownership	2.19	0.1
8. Trust	0.95	—
9. Society Registered Under Societies Act, 1860	0.30	—
	1864.68*	100.0

* Including Agency Fund loans in the case of Punjab Financial Corporation.

V.2. Private and public limited companies together account for 57% of the amount, and partnerships another 27%. Proprietary concerns have got almost an eighth of the total. Co-operatives make a poor impression.

V.3. Data regarding the breakdown of sanctions, as against outstandings, obtained from SFCs as on 31st December, 1962, show a broadly similar picture as above. Public and private limited concerns got 63%; partnerships—23%; proprietary concerns—11%; joint Hindu undivided family concerns—2%; and co-operatives—1%. The inclusion of MIIC sanctions with these only increases the limited companies' share to 67%, reducing the shares of partnerships and proprietary concerns by 2% each.

V.4. These all-India averages conceal quite wide inter-State differences. The share of private limited companies, which, in the aggregate, account for 30.4% of the outstandings for all SFCs, ranges from 59% in Maharashtra to 3.9% in Jammu and Kashmir. For public limited companies, the range around the general aggregate share of 26.7% is even wider—even barring Jammu and Kashmir where the figure is nil, it varies from 62% in Rajasthan to 11.5% in Bombay; even West Bengal has recorded only 49.5% in this category and Bihar 58.4%. With such variations in these two categories, variations under partnerships are much less pronounced around the all-India figure of 26.8%; they range from 12% in West Bengal to 39.6% in Gujarat (omitting Jammu and Kashmir where the ratio of 95% is inconclusive as the total amount is very small). Hindu undivided families have been prominent only in Madhya Pradesh, Mysore and Andhra, and co-operatives in Andhra.

V.5 Thus, subject to such inter-State variations which must often be explained by the character and predilections of management more than by the basic environment of economic forces in which SFCs operate, the intentions of the framers of the Act, namely, that concerns other than public limited companies may also be accommodated, have been generally satisfied. But there is a trend towards public limited companies whose share in outstandings rose from 26.7% at the end of 1961-62 to 29.5% at the end of 1962-63. Proprietary and partnership concerns shared the loss.

Breakdown by size of industiral concern

V.6. One of the objectives in enacting the SFCs Act to set up these State-level Corporations was to cater to the needs of medium and small scale units. This was further buttressed by limiting the total guarantee plus loans facility to a concern to 10% of the paid-up capital of SFCs and in any case to a maximum of Rs. 10 lakhs. By an amendment in 1962, the link with paid-up capital was removed; the ceiling now is Rs. 20 lakhs for public limited companies and co-operatives, but Rs. 10 lakhs for all others.

V.7. For some years, SFCs have been submitting to Reserve Bank the breakdown of their loans and advances into those to large, medium and small scale units, according to assets, for this purpose assets being taken "to mean those which are used for working the industry". Units with assets of over Rs. 20 lakhs were large scale; those with more than Rs. 5 lakhs but not exceeding Rs. 20 lakhs were medium units; and those with less than Rs. 5 lakhs and employing less than 50 workers if working with power or less than 100 workers if working without power were small scale units. The Government of India's definition of a small unit was changed—once in May, 1959 and again in March, 1960. It is now defined as a unit with a capital investment of not more than Rs. 5 lakhs, irrespective of the number employed; for this definition, capital investment was stated to mean investment in fixed assets like land, buildings, machinery

and equipment; where units are functioning in rented premises, the capital valuation of such buildings shall be taken into account in assessing the prescribed limit of Rs. 5 lakhs, excluding workers' housing and welfare amenities; also, to calculate the value of machinery and equipment, the original price paid by the owner, irrespective of whether it was new machinery and equipment or secondhand, will be taken.

Breakdown of loans outstanding—according to size—as on 31st March, 1962.

Classification according to size	Amount (Rs. lakhs)	%
1. Large scale	488.21	26.2
2. Medium scale	853.25	45.8
3. Small scale	523.22	28.0
	1864.68	100.0

V.8. Of the total outstanding loans of Rs. 18.65 crores as on the above date, large scale units had 26.2%, medium scale units, 45.8%, and small scale units, 28%. Or, against 28% outstanding from small units, larger units accounted for 72%. These proportions vary a great deal from one SFC to another. Barring Jammu & Kashmir, where the entire amount is outstanding from small units (the total amount outstanding is, however, vary small, viz., Rs. 6.46 lakhs), the overall ratio of 26.2% for large units varies from 4.2% in Punjab and 13.3% in Bombay to 44% in West Bengal, 45.5% in Uttar Pradesh, 48.9% in Gujarat and as much as 58.4% in a relatively underdeveloped State like Rajasthan. This pattern is often the counterpart of the earlier one, viz., the breakdown according to the constitution of industrial units. The small amount to large scale units in Punjab must be related to the small proportion going to public limited companies, and to fully 75% going to partnerships and private limited companies. The very high figure for Rajasthan only reflects that almost two-thirds are due from public limited companies in that State. In Maharashtra where only 13.3% are due from large units, fully 52% and 27% are due from private limited and partnership concerns, less than 12% being from public limited concerns.

V.9. In the case of medium scale units as well, there are considerable variations around the all-SFCs average of 45.8%. Madhya Pradesh, Rajasthan and Uttar Pradesh fall in the 21-30% range; Andhra, Gujarat and Mysore in the 31-40% range; Bihar, West Bengal, Orissa and Kerala in the 41-50% range; and Assam, Maharashtra and Punjab in the 51-60% range.

V.10. For small units—all-SFCs average 28%—Jammu and Kashmir occupies the first place—100%. West Bengal, with 8.3% is solitary in

the 1-10% range; in the 11-20% range fall Rajasthan and Gujarat; in the 21-30% range fall Bihar, Assam, Uttar Pradesh, Kerala and Maharashtra; in the 31-40% range are Madhya Pradesh, Andhra and Punjab; next are Mysore—47% and Orissa—51%.

V.11. But for the exhortations from various quarters, the share of small scale units would have been even less than the 28% observed for loans outstanding on 31st March, 1962. With these exhortations, the management of these SFCs have diverted more of their sanctions to this sector. Thus, in March, 1959 only 20% of the amounts sanctioned by eleven SFCs then working was for small units. In the next three years, this ratio improved to 23.8%, 29.0% and 31.1% (in March 1962). Nevertheless, the total sanctions to small units by SFCs were only Rs. 10.69 crores in March 1962, of which over one-half was contributed by Punjab and Andhra.

V.12. Before taking up a more detailed discussion of the size of loans, we may look at the size aspect in relation to the size of units. As on 31st

Average amount sanctioned per application
(all SFCs)

(Rs. '000)

Sanction to	As on				% increase in 31-3-62 over 31-3-59
	31-3-59	31-3-60	31-3-61	31-3-62	
(*i*) Small units	77.4	83.4	85.3	84.3	9
(*ii*) Other units	340.1	370.4	432.8	441.3	30

March, 1962, the State-wise averages for small units range from Rs. 1.47 lakhs in West Bengal and Rs. 1.28 lakhs in Punjab to Rs. 0.56 lakh in Andhra. Similarly, for other (i.e. not small—a convenient abbreviation which we shall use below) units, they range from Rs. 8.38 lakhs in Madhya Pradesh to Rs. 3.42 lakhs and Rs. 3.62 lakhs in Punjab and Orissa respectively. It is significant that while the size of the average sanction to a small unit has increased by 9% between March, 1959 and 1962, that to an "other unit" has increased by fully 30%.

V.13. The average size of sanctions to small units has risen little so far. But, given the conservative practices of some SFCs in evaluating fixed assets, and keeping a sufficient margin in sanctioning loans, the absolute size of these sanctions—Rs. 0.84 lakh in March, 1962—perhaps shows that at least in some States, the smaller concerns of which the assets are not in the six-figure category are yet not accommodated.

V.14. As stated earlier, an amendment of the Act effective from the 16th April, 1962, raised the limit of accommodation by a SFC to a public limited or co-operative concern from Rs. 10 lakhs to Rs. 20 lakhs. SFCs were requested for data showing applications and sanctions of over Rs. 10

lakhs (including those for additional loans from units which had been already assisted upto Rs. 10 lakhs). These data are shown below, broken down into those for 1962-63 and for April-August, 1963.

Larger loans sanctioned after SFCs Amendment Act, 1962.

(Rs. lakhs)

	1962-63	April-August, 1963	Total
1. Number of applications received	63*	25	88
2. Amount applied for	1057.68*	411.00	1468.68
3. Number of applications sanctioned	31*@	13	44
4. Amount sanctioned	412.05*@	194.19	606.24
5. Amount sanctioned to *new* units	171.25	121.80	293.05
6. Amount sanctioned to *existing* units for extension/modernisation	240.80*	72.39	313.19
7. Of 6, amount sanctioned to units to which loans upto Rs. 10 lakhs had been sanctioned before SFCs Amendment Act, 1962	118.80*	3.15	121.95

* Includes one for Rs. 5 lakhs to a co-operative society
@ Two sanctions amounting to Rs. 30 lakhs since cancelled.

Thus, in 1962-63 alone, SFCs sanctioned Rs. 4.12 crores of these larger loans. This is as much as 28% of all sanctions in that year. The average value of sanctions is over Rs. 13 lakhs. The tempo of these sanctions seems to have gone up since. In the first five months of 1963-64 another Rs. 1.94 crores of such loans were sanctioned, the average value of sanctions being Rs. 15 lakhs.

V.15. All these sanctions, except one for Rs. 5 lakhs granted in Andhra Pradesh to a co-operative society which had earlier got Rs. 10 lakhs, are to public limited companies. It is of interest that almost one-half of these sanctions was to new units, and the rest to existing units, for expansion or modernisation.

V.16. Of the sanctions of Rs. 6.06 crores upto August, 1963, well over one-half was contributed by three SFCs: Madhya Pradesh—Rs. 1.44 crores, Maharashtra—Rs. 1.05 crores, and West Bengal—Rs. 1.03 crores.

Purpose-wise breakdown of loans

V.17. An "industrial concern", with which a SFC can carry on and transact the different kinds of business detailed in Sec. 25 of the SFCs Act, has been defined in Sec. 2(*c*) as:

> "any concern engaged or to be engaged in the manufacture, preservation or processing of goods or in mining or in the hotel industry or in the transport of passengers or goods by road or by water or in the generation or distribution of electricity or any other form of power or in the development of any contiguous area of land as an industrial estate."

The expression "processing of goods" is stated to include any art or process for producing, preparing or making an article by subjecting any material to a manual, mechanical, chemical, electrical or any other like operation. The words "or to be engaged" in the above definition were added by Act 28 of 1955. Act 56 of 1956 added the explanation of "processing of goods". Act 6 of 1962 (30th March, 1962) widened the earlier definition of "industrial concern" to include concerns engaged (*a*) in the hotel industry or (*b*) in the transport of passengers or goods by road or by water or (*c*) in the development of any contiguous area of land as an industrial estate. Even before this amendment, SFCs were empowered to finance a large variety of industrial undertakings. Their actual performance in this regard upto March, 1963, may now be examined.

V.18. Industry-wise i.e. purpose-wise breakdown of outstanding loans is usually reported by the Corporations to Reserve Bank every quarter. From these returns, a summary table has been drawn up—Table IX—showing the industry-wise breakdown of loans and advances, separately for SFCs and MIIC, as also for all the Corporations, outstanding at the end of March, 1962 and March, 1963. The loan operations of the Corporations during 1962-63 seem to have contributed to a slightly greater diversification among industries as compared with the position as at the end of 1961-62. Food manufacturing and textiles may be taken to fall largely in the "traditional" group of industries. The likely exception may be "cold storages" under the "Food" group, which are relatively new types of ventures, helping storage of grains and other foodstuffs to facilitate their orderly marketing over the entire year; but loans for cold storages account for less than 5% of the total outstandings of the Corporations at the end of 1962-63. This traditional group of industries can be distinguished from the significant assortment of other industries which may be called "non-traditional" industries—chemicals, basic metal and metal manufacturing industries, paper and paper products, machinery, etc. The former group accounted for 43.56% and 40.63% of the outstandings of the Corporations at the end of March, 1962 and March, 1963 respectively. Even this 3% reduction permitted fair amounts of increase in many industries in the latter group as the total outstandings increased by no less than 37% during 1962-63. The extent of diversification would be more evident from data relating to SFCs alone, as in their case the decline under the "traditional" industries group is a little more than for MIIC.

V.19. Table X presents more detailed, Corporation-wise, information on outstanding advances at the end of March, 1963. It is in two parts—outstandings with A: small units, and B: other units, showing the major industries and the more important States against each major industry group. This is examined below.

V.20. Advances to small units—On 31st March, 1963, the outstanding loans of SFCs to small scale units were Rs. 671 lakhs. If loans of

TABLE IX

Major industry-wise loans and advances (outstanding) as at the end of March, 1962 and 1963.

(Rs. Lakhs)

Major industries groups	14 State Financial Corporations				Madras Industrial Investment Corporation Ltd.				All 15 Corporations			
	As at the end of March, 1962		As at the end of March, 1963		As at the end of March, 1962		As at the end of March, 1963		As at the end of March, 1962		As at the end of March, 1963	
	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
1. Food Manufacturing Industries except Beverages (Total)	452.86	24.86	529.37	21.39	79.01	11.77	90.83	9.81	531.87	21.38	620.20	18.23
(*i*) Sugar	85.51	(4.69)	88.36	(3.57)	19.00	(2.83)	19.00	(2.05)	104.51	(4.20)	107.36	(3.15)
(*ii*) Tea	88.24	(4.85)	119.96	(4.85)	—	—	—	—	88.24	(3.55)	119.96	(3.53)
(*iii*) Cold Storage	132.48	(7.27)	154.57	(6.24)	—	—	—	—	132.48	(5.33)	154.57	(4.54)
(*iv*) Others	146.63	(8.05)	166.48	(6.73)	60.01	(8.94)	71.83	(7.76)	206.64	(8.30)	238.31	(7.01)
2. Manufacture of Textiles (Total)	243.70	13.38	335.60	13.56	307.95	45.88	426.39	46.05	551.65	22.18	761.99	22.40
(*i*) Cotton Textiles	124.10	(6.81)	218.43	(8.83)	307.95	(45.88)	426.39	(46.05)	432.05	(17.37)	644.82	(18.96)
(*ii*) Others	119.60	(6.57)	117.17	(4.73)	—	—	—	—	119.60	(4.81)	117.17	(3.44)
3. Manufacture of Wood & Cork	46.82	2.57	56.97	2.30	—	—	—	—	46.82	1.88	56.97	1.67
4. Manufacture of Furniture, etc.	—	—	27.44	1.11	—	—	—	—	—	—	27.44	0.81
5. Manufacture of Paper and Paper Products	63.18	3.47	100.06	4.04	1.58	0.24	25.02	2.70	64.76	2.60	125.08	3.68
6. Printing, Publishing, etc.	34.55	1.90	50.98	2.06	16.50	2.46	16.50	1.78	51.05	2.05	67.48	1.98

7. Manufacture of Rubber Products	31.73	1.74	41.15	1.66	6.79	1.01	7.57	0.82	38.52	1.55	48.72	1.43
8. Manufacture of Chemicals & Chemical Products (Total)	159.06	8.73	230.26	9.30	30.33	4.52	36.49	3.93	189.39	7.61	266.75	7.84
(*i*) Basic Chemicals	37.77	(2.07)	44.36	(1.79)	21.49	(3.20)	23.18	(2.50)	59.26	(2.38)	67.54	(1.99)
(*ii*) Paints & Varnishes	—	—	16.51	(0.67)	—	—	0.90	—	—	—	17.41	(0.51)
(*iii*) Drugs & Pharmaceuticals	43.96	(2.41)	55.58	(2.24)	0.50	—	2.24	(0.24)	44.46	(1.79)	57.82	(1.70)
(*iv*) Others	64.43	(3.54)	113.81	(4.60)	7.44	(1.11)	10.17	(1.10)	71.87	(2.89)	123.98	(3.64)
9. Manufacture of Non-metallic Mineral Products	123.80	6.80	167.22	6.76	24.68	3.68	31.10	3.36	148.4[illegible]	5.97	198.32	5.83
10. Basic Metal Industries (Total)	121.95	6.70	218.69	8.84	10.49	1.56	23.17	2.50	132.44	5.32	241.86	7.11
(*i*) Iron & Steel Basic Industries	116.55	(6.40)	208.58	(8.43)	9.74	(1.45)	23.17	(2.50)	126.29	(5.08)	231.75	(6.81)
(*ii*) Others	5.40	(0.30)	—	—	0.75	—	—	—	6.15	(0.24)	—	—
11. Manufacture of Metal Products except Machinery and Transport Equipment	88.71	4.87	134.11	5.42	8.00	1.19	8.00	0.86	96.71	3.89	142.11	4.18
12. Manufacture of Machinery except Electrical Machinery	136.60	7.50	177.33	7.16	62.38	9.29	110.43	11.93	198.98	8.00	287.76	8.46
13. Manufacture of Electrical Machinery	54.97	3.02	89.26	3.61	33.95	5.06	47.63	5.14	88.92	3.57	136.89	4.02
14. Manufacture of Transport Equipment	86.15	4.73	121.11	4.89	19.50	2.91	27.45	2.96	105.65	4.25	148.56	4.37
15. Electricity, Gas, Water & Sanitary Services	34.[illegible]	1.89	39.14	1.58	52.00	7.45	55.50	5.99	86.48	3.48	94.64	2.78
Total for all industries (including certain minor industries not enumerated above)	1,820.75		2476.27		669.31		928.92		2490.06		3405.19	

NOTE: Percentages relate to Total.

TABLE X–A

Major industry-wise loans and advances (outstanding) as on 31st March, 1963—Small scale industries—Contd.

(Rs. lakhs)

Major industry-wise breakdown	Total for SFCs and MIIC	Total-14 SFCs	% of (2) to total	% of (3) to total	Andhra Pradesh	Assam	Bihar	Gujarat	Jammu & Kashmir	Kerala
(1)	(2) Rs.	(3) Rs.	(4)	(5)	(6) Rs.	(7) Rs.	(8) Rs.	(9) Rs.	(10) Rs.	(11) Rs.
1. Food Manufacturing Industries except Beverages (Total)	179.37	171.86	25.5	25.6	12.20 (6.8)	24.49 (13.7)	26.71 (14.9)	—	—	12.93 (7.2)
(*i*) Tea	18.09	18.09	2.6	2.7	—	15.75 (8.8)*	—	—	—	—
(*ii*) Cold Storage	79.51	79.51	11.3	11.8	—	—	24.66 (13.7)*	—	—	—
(*iii*) Miscellaneous Food Preparations	76.33	68.82	10.8	10.3	—	—	—	—	—	10.59 (5.9)*
2. Manufacture of Textiles (Total)	32.64	32.64	4.6	4.9	—	—	—	—	—	3.03 (9.3)
(*i*) Cotton Textiles	13.51	13.51	1.9	2.0	—	—	—	—	—	—
(*ii*) Others	19.13	19.13	2.7	2.9	—	—	—	—	—	2.23 (6.8)*
3. Manufacture of Wood and Cork except manufacture of Furniture	27.17	27.17	3.9	4.0	—	18.65 (68.6)	—	—	—	2.[illegible] (8.8)
4. Manufacture of Paper and Paper Products	17.05	14.80	2.4	2.2	2.88 (16.9)	—	—	1.68 (9.9)	—	—

5. Printing, Publishing, etc.	32.39	30.14	4.6	4.5	3.25 (10.0)	5.50 (17.0)	—	—	—	—
6. Rubber Products	15.95	12.38	2.3	1.8	—	—	—	—	—	5.92 (37.1)
7. Manufacture of Chemicals (Total)	48.14	41.20	6.8	6.1	6.91 (14.4)	—	—	—	—	—
(*i*) Basic Chemicals	14.30	13.00	2.0	1.9	5.59 (11.6)*	—	—	—	—	—
(*ii*) Drugs ■ Pharmaceuticals	12.71	10.47	1.8	1.6	—	—	—	—	—	—
(*iii*) Others	17.63	15.13	2.5	2.3	—	—	—	—	—	—
8. Manufacture of Non-metallic Mineral Products	54.28	54.28	7.7	8.1	—	—	5.04 (9.3)	4.52 (8.3)	—	4.34 (8.0)
9. Basic Metal Industries	74.71	67.54	10.6	10.1	—	—	6.90 (9.2)	6.13 (8.2)	—	—
(*i*) Iron & Steel Basic Industries	71.33	64.16	10.1	9.6	—	—	6.90 (9.2)*	5.13 (6.9)*	—	—
10. Manufacture of Metal Products	63.71	63.71	9.0	9.5	4.59 (7.2)	6.14 (9.6)	—	—	—	—
11. Manufacture of Machinery except Electrical Machinery	40.78	40.78	5.8	6.1	—	—	—	—	—	—
12. Manufacture of Electrical Machinery	23.65	21.76	3.4	3.2	1.69 (7.1)	—	—	1.57 (6.6)	—	—
13. Manufacture of Transport Equipment	21.41	21.41	3.0	3.2	1.87 (8.7)	2.15 (10.0)	2.11 (10.0)	—	—	—
14. Miscellaneous	71.22	71.22	—	—			(State-wise breakdown not indicated)			
Total	702.47	670.89			51.37	72.27	48.74	20.32	8.10	35.20

TABLE X-A

Major industry-wise loans and advances (outstanding) as on 31st March, 1963—Small scale industries—Concluded.

(Rs. lakhs)

Major industry-wise breakdown	Madhya Pradesh	Maha-rashtra	Mysore	Orissa	Punjab	Rajas-than	Uttar Pradesh	West Bengal	MIIC
(1)	(12) Rs.	(13) Rs.	(14) Rs.	(15) Rs.	(16) Rs.	(17) Rs.	(18) Rs,	(19) Rs.	(20) Rs.
1. Food Manufacturing Industries except Beverages (Total)	—	—	—	18.20 (10.1)	27.39 (15.3)	—	18.29 (10.2)	—	—
(*i*) Tea	—	—	—	—	—	—	—	—	—
(*ii*) Cold Storage	—	—	—	—	18.96 (10.6)*	—	14.69 (8.2)*	—	—
(*iii*) Miscellaneous Food Preparations	—	—	—	12.21 (6.8)*	—	—	—	—	—
2. Manufacture of Textiles (Total)	4.15 (12.7)	6.70 (20.5)	5.64 (17.3)	—	7.62 (23.3)	—	—	—	—
(*i*) Cotton Textiles	3.61 (11.1)*	2.36 (7.2)*	2.38 (7.3)*	—	1.70 (5.2)*	—	—	—	—
(*ii*) Others	—	4.34 (13.3)*	3.26 (10.0)*	—	5.92 (18.1)*	—	—	—	—
3. Manufacture of Wood and Cork except manufacture of Furniture	—	2.86 (10.5)	—	—	—	—	—	—	—
4. Manufacture of Paper and Paper Products	1.72 (10.1)	4.72 (27.7)	—	—	3.30 (19.4)	—	—	—	—
5. Printing, Publishing, etc.	—	10.23 (31.6)	—	2.66 (8.2)	—		4.18 (12.9)	2.65 (8,2)	2.25 (6.9)

6. Rubber Products	—	—	1.85 (11.6)	—	1.50 (9.4)	—	—	1.25 (7.8)	3.57 (22.4)
7. Manufacture of Chemicals (Total)	—	16.69 (34.6)	—	—	—	—	—	—	6.94 (14.4)
(*i*) Basic Chemicals	—	—	—	—	—	—	—	—	—
(*ii*) Drugs & Pharmaceuticals	—	6.49 (13.5)*	—	—	—	—	—	—	—
(*iii*) Others	—	7.32 (15.2)*	—	—	—	—	—	—	2.50 (5.2)*
8. Manufacture of Non-metallic Mineral Products	—	5.17 (9.5)	15.26 (28.1)	5.10 (9.4)	5.86 (10.8)	—	—	—	—
9. Basic Metal Industries	7.57 (10.1)	6.48 (8.7)	11.94 (16.0)	—	10.14 (13.6)	—	—	6.36 (8.5)	7.17 (9.6)
(*i*) Iron & Steel Basic Industries	6.97 (9.3)*	4.75 (6.4)*	11.94 (16.0)*	—	10.14 (13.6)*	—	—	6.36 (8.5)*	7.17 (9.6)*
10. Manufacture of Metal Products	6.01 (9.4)	29.40 (46.1)	—	—	5.02 (7.9)	4.76 (7.5)	—	—	—
11. Manufacture of Machinery except Electrical Machinery	—	11.78 (28.9)	—	—	11.55 (28.3)	—	5.37 (13.2)	—	—
12. Manufacture of Electrical Machinery	—	7.68 (32.5)	—	—	4.02 (17.0)	2.92 (12.3)	—	2.00 (8.5)	1.89 (8.0)
13. Manufacture of Transport Equipment	2.51 (11.7)	—	—	—	8.13 (38.0)	—	1.89 (8.7)	—	—
14. Miscellaneous	(State-wise breakdown not indicated)								
Total	42.08	125.64	53.89	32.40	101.25	17.63	35.63	26.39	31.58

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TABLE X-B

*Major industry-wise loans and advances (outstanding) as on 31st March, 1963—Other industries—*Contd.

(Rs. lakhs)

Major industry-wise breakdown	Total for SFCs and MIIC	Total-14 SFCs	% of (2) to total	% of (3) to total	Andhra Pradesh	Assam	Bihar	Gujarat	Kerala
(1)	(2) Rs.	(3) Rs.	(4)	(5)	(6) Rs.	(7) Rs.	(8) Rs.	(9) Rs.	(10) Rs.
1. Food Manufacturing Industries except Beverages (Total)	440.83	357.51	16.3	19.8	34.20 (7.8)	81.12 (18.4)	61.92 (14.0)	—	37.76 (8.6)
(i) Sugar	101.92	82.92	3.8	4.6	—	—	37.70 (8.6)*	—	—
(ii) Tea	101.87	101.87	3.8	5.6	—	65.40 (14.8)*	—	—	27.97 (6.3)*
(iii) Cold Storage	75.06	75.06	2.8	4.2	—	—	—	—	—
(iv) Miscellaneous Food Preparations	161.98	97.66	5.9	5.4	25.20 (5.7)*	—	—	—	—
2. Manufacture of Textiles (Total)	729.35	302.96	27.0	16.8	37.42 (5.1)	—	—	—	—
(i) Cotton Textiles	631.31	204.92	23.4	11.4	—	—	—	—	—
(ii) Others	98.04	98.04	3.6	5.4	—	—	—	—	—
3. Manufacture of Wood & Cork except Manufacture of Furniture	29.80	29.80	1.1	1.7	—	13.87 (46.5)	—	—	7.41 (24.9)
4. Manufacture of Furniture	16.76	16.76	0.6	0.9	—	—	—	—	—
5. Manufacture of Paper and Paper Products	108.03	85.26	4.0	4.7	—	—	19.90 (18.4)	10.00 (9.3)	—

6. Printing, Publishing, etc.	35.09	20.84	1.3	1.2	—	—	—	—	—
7. Manufacture of Rubber Products	32.77	28.77	1.2	1.6	—	—	—	—	10.78 (32.9)
8. Manufacture of Chemicals (Total)	218.61	189.06	8.1	10.5	23.95 (11.0)	—	—	22.15 (10.1)	—
(*i*) Basic Chemicals	53.24	31.36	2.0	1.7	—	—	—	—	—
(*ii*) Paints and Varnishes	13.91	13.91	0.5	0.8	—	—	—	—	—
(*iii*) Drugs and Pharmaceuticals	45.11	45.11	1.7	2.5	—	—	—	—	—
(*iv*) Others	106.35	98.68	3.9	5.5	16.59 (7.6)*	—	—	22.15 (10.1)*	—
9. Manufacture of, Non-Metallic Mineral Products	144.04	112.94	5.3	6.3	—	10.00 (6.9)	17.18 (11.9)	—	15.96 (11.1)
10. Basic Metal Industries	167.15	151.15	6.2	8.4	—	17.13 (10.2)	24.26 (14.5)	—	—
(*i*) Iron and Steel Basic Industries	160.42	144.42	5.9	8.0	—	17.13 (10.2)*	21.01 (12.6)*	—	—
11. Manufacture of Metal Products	78.40	70.40	2.9	3.9	—	—	—	—	—
12. Manufacture of Machinery except Electrical Machinery	246.98	136.55	9.1	7.6	—	—	—	—	—
13. Manufacture of Electrical Machinery	113.24	67.50	4.2	3.7	—	—	—	—	—
14. Manufacture of Transport Equipment	127.15	99.70	4.7	5.5	—	18.50 (14.5)	19.90 (15.7)	—	—
15. Electricity, Gas, Water and Sanitary Services	91.88	36.38	3.4	2.0	—	20.27 (22.1)	6.98 (7.5)	—	—
16. Miscellaneous	122.64	99.80	—	—	(State-wise breakdown not indicated)				
Total	2,702.72	1,805.38			110.05	174.22	159.16	69.21	126.84

NOTE: Figures in brackets are percentages to total loans outstanding for all the Corporations in the respective industry-wise group indicated in (2).

* Figures are represented as percentage of the total in the respective *main* group.

TABLE X-B

Major industry-wise loans and advances (outstanding) as on 31st March, 1963—Other industries—Concluded.

(Rs. lakhs)

Major industry-wise breakdown	Madhya Pradesh	Maha-rashtra	Mysore	Orissa	Punjab	Rajas-than	Uttar Pradesh	West Bengal	MIIC
(1)	(11)	(12)	(13)	(14)	(15)	(16)	(17)	(18)	(19)
	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.
1. Food Manufacturing Industries except Beverages (Total)	—	—	—	—	—	—	27.26 (6.2)	47.12 (10.7)	[illegible].32 (18.9)
(*i*) Sugar	—	—	—	—	—	—	—	—	—
(*ii*) Tea	—	—	—	—	—	—	—	—	—
(*iii*) Cold Storage	—	—	—	—	—	—	—	28.62 (6.5)*	—
(*iv*) Miscellaneous Food Preparations	—	—	—	—	—	—	—	—	64.32 (14.6)*
2. Manufacture of Textiles (Total)	—	—	34.92 (4.8)	—	—	41.20 (5.6)	—	39.09 (5.4)	426.39 (58.5)
(*i*) Cotton Textiles	—	—	34.92 (4.8)*	—	—	—	—	39.09 (5.4)*	426.39 (58.5)*
(*ii*) Others	—	—	—	—	—	—	—	—	—
3. Manufacture of Wood & Cork except manufacture of Furniture	—	2.52 (8.5)	—	—	—	—	—	6.00 (20.1)	—
4. Manufacture of Furniture	—	16.76 (100.0)	—	—	—	—	—	—	—
5. Manufacture of Paper and Paper Products	9.30 (8.6)	10.79 (10.0)	—	—	10.95 (10.1)	—	12.74 (11.5)	9.75 (9.0)	22.77 (21.1)
6. Printing, Publishing, etc.	—	—	—	2.10 (6.0)	—	—	—	14.41 (41.1)	14.25 (40.6)
7. Manufacture of Rubber Products	—	9.46 (28.9)	—	—	3.60 (11.0)	—	—	4.93 (15.0)	—

8. Manufacture of Chemicals (Total)	11.95 (5.5)	84.81 (38.8)	—	—	—	—	—	28.35 (13.0)	29.55 (13.5)
(i) Basic Chemicals	—	17.18 (7.9)*	—	—	—	—	—	—	21.88 (10.0)*
(ii) Paints and Varnishes	—	11.36 (5.2)*	—	—	—	—	—	—	—
(iii) Drugs and Pharmaceuticals	—	31.13 (14.2)*	—	—	—	—	—	—	—
(iv) Others	11.95 (5.5)*	25.14 (11.5)*	—	—	—	—	—	14.30 (6.5)*	—
9. Manufacture of Non-metallic Mineral Products	—	14.71 (10.2)	—	7.00 (4.9)	14.60 (10.1)	7.27 (5.1)	—	16.93 (11.8)	31.10 (21.6)
10. Basic Metal Industries	16.35 (9.8)	—	—	—	47.98 (28.7)	14.52 (8.7)	—	—	16.00 (9.6)
(i) Iron and Steel Basic Industries	16.35 (9.8)*	—	—	—	44.50 (26.6)*	14.52 (8.7)*	—	—	16.00 (9.6)*
11. Manufacture of Metal Products	—	28.96 (36.9)	—	—	—	—	10.80 (13.8)	19.55 (24.9)	8.00 (10.2)
12. Manufacture of Machinery except Electrical Machinery	—	36.29 (14.7)	—	—	43.72 (17.7)	—	—	23.00 (9.3)	110.43 (44.7)
13. Manufacture of Electrical Machinery	—	20.06 (17.7)	—	—	—	—	—	33.01 (29.2)	45.74 (40.4)
14. Manufacture of Transport Equipment	—	6.62 (5.2)	—	—	33.50 (26.3)	—	—	6.66 (5.3)	27.45 (21.6)
15. Electricity, Gas, Water and Sanitary Services	—	—	—	—	—	—	—	—	55.50 (60.4)
16. Miscellaneous	(State-wise breakdown not indicated)								
Total	109.28	282.96	59.85	38.37	232.80	98.32	85.23	259.09	897.34

NOTE: Figures in brackets are percentages to total loans outstanding for all the Corporations in the respective industry-wise group indicated in (2)

* Figures are represented as percentage of the total in the respective *main* group.

Rs. 32 lakhs outstanding from small units to MIIC on that day are also included, the total is Rs. 703 lakhs. Table X-A shows that one quarter of this falls in one industry group, viz., "Food Manufacturing Industries except Beverages", which is almost fully accounted for by cold storage, and miscellaneous food preparations, leaving a small amount against tea manufacturing.

V.21. Leaving the food group as also textiles on one side, there is an interesting assortment of advances to what may be called, perhaps, "non-traditional" industries, to distinguish them from the "traditional" industries of food manufacturing, etc. and textiles, some of the more important of which are shown below:

		% to total outstanding	
		SFCs.	SFCs & MIIC
(i)	Manufacture of chemicals and chemical products	6.1	6.8
(ii)	Manufacture of non-metallic mineral products—except products of petroleum and coal	8.1	7.7
(iii)	Basic metal industries: Iron and steel basic industries	9.6	10.1
(iv)	Manufacture of metal products except machinery and transport equipment	9.5	9.0
(v)	Manufacture of machinery except electrical machinery	6.1	5.8

(Groups to which advances outstanding are less than 5% of the total are not included here—some of these are: Printing, publishing, etc; manufacture of electrical machinery, apparatus, appliances and supplies; and manufacture of transport equipment).

V.22. Though the absolute amounts outstanding with small scale units are small, the spread of business to these sectors is encouraging, and needs to be stepped up rapidly.

V.23. Nevertheless, from a discussion of certain details of these advances in the Appendix, it is permissible to draw the conclusion that, whatever be the reasons for it, in advancing loans to small units, the Corporations have generally stuck to the more "traditional" industries and to industries for which the processes of production are relatively simple, and do not require detailed scrutiny of the proposals at a relatively advanced level of technical expertise, and for which machinery as well as raw materials are more readily available, often internally.

V.24. Advances to other units—On 31st March, 1963, the outstanding loans of SFCs to "Other", i.e. medium and large-sized, industrial concerns were Rs. 18.05 crores; including loans of Rs. 8.97 crores of MIIC outstanding with such units on that date, the total is Rs. 27.02 crores.

V.25. As in the case of advances to small units, loans in the group "Food Manufacturing Industries" account for 20 per cent of the total for SFCs, and 16 per cent of the total for all 15 Corporations. The total

amount in this group is well distributed among sugar, tea, cold storage and miscellaneous food preparations.

V.26. The next most important group, in this case very much more important than for small units, is textiles which have taken up 17% of the outstandings of SFCs. If the large sum—Rs. 426 lakhs—shown against MIIC be included, the importance of this group to the total is enhanced to 27% which is more than the share of the food group to the total. These two groups thus account for 43% of the total for fifteen Corporations, or 37% of the total for SFCs. The corresponding figures for advances to small units are smaller—30% and 31% respectively.

V.27. Leaving these two groups on one side, there is also in this "Other" units' sector, as in the small units' sector, an assortment of what was termed above as "non-traditional" industries:

		% of total outstanding	
		SFCs	SFCs & MIIC
(i)	Manufacture of chemicals and chemical products	10.5	8.1
(ii)	Manufacture of machinery except electrical machinery	7.6	9.1
(iii)	Manufacture of non-metallic mineral products	6.3	5.3
(iv)	Basic metal industries, of which	8.4	6.2
	iron and steel basic industries	8.0	5.9
(v)	Manufacture of transport equipment	5.5	4.7
(vi)	Manufacture of paper and paper products	4.7	4.0
(vii)	Manufacture of metal products except machinery and transport equipment	3.9	2.9
(viii)	Manufacture of electrical machinery	3.7	4.2

As in the case of small units, certain details of advances to "Other" units are discussed in the Appendix.

V.28. A few general remarks—No very detailed analysis of the Corporations' loans and advances has been attempted here, and the effort has been conducted in terms of the outstandings and not of sanctions, which may reveal a somewhat different pattern. It seems that viewed against the background of even such limited measure of diversification of the industrial structure of India which has been attained since Independence, these Corporations have not contributed significantly to this achievement. For some reasons, they have, with a few notable exceptions, shied away from the newly developing industries (of course, all States do not offer comparable facilities for these industries). What could be those reasons? One cannot be very specific in answering this question. But it is possible to point to a few factors, although their precise relative importance may not be determinate, which may have affected the working of the Corporations. One of these was indirectly mentioned

above—viz., the, perhaps, understandable inclination of their management to take up for assistance units in such industries for which the processes of production are relatively simple, and do not require very detailed scrutiny of the proposals at an advanced level of technical expertise. But this itself may be the result of four other considerations: (*a*) the lack of technically qualified persons on the staff of these Corporations to appraise proposals from the less well-known sectors of industrial activity, or of sufficiently effective arrangements for such appraisal by outside bodies; (*b*) in most cases, applications from "non-traditional" sectors would be, ex definitione, from newly set-up units, often yet to be engaged in manufacture—but it was not till 1955 that industrial units "to be engaged" in manufacture, etc. were eligible for assistance from SFCs; (*c*) as the financing of "non-traditional" industries sometimes entails more risks, SFCs with their meagre resources and deadweight of subvention liabilities may have preferred to concentrate on safer business instead of branching out into unknown fields; and (*d*) the absence of underwriting and of direct subscription to the equity of borrowing concerns—facilities which newly set-up units greatly value, and the provision of which must have contributed significantly to the success of ICICI in directing much of its assistance into the newly developing sectors of industry which also seem to possess a high growth potential. But the success of ICICI is also due to a few other factors, viz., large scale operation, availability of foreign exchange, and of a large, long term, interest-free loan from Government—none of which applies to SFCs. The availability of foreign exchange often holds the key to starting industrial units in most of what was designated as the "non-traditional" sector of industry. The availability of the interest-free loan emboldened ICICI into financing new units and taking up their shares which may give little or no returns in the first few years; the dividend paying capacity of ICICI itself was fully underwritten by the returns on the interest-free loan.

V.29. Notwithstanding these adverse factors—for remedying some of which certain recommendations have been made elsewhere in the Report, the desirability of SFCs diverting more resources into industries with a marked growth-potential must be accepted. Apart from the characteristics of these latter types of industries which differentiate them from the older, "traditional" industries, such a shift may also be needed as most of the assistance provided by SFCs goes not to public limited companies but to proprietary, partnership, joint Hindu family, and private limited concerns, which are generally smaller than the former, and often suffer from many disabilities that go with smallness, and put brakes on a faster rate of growth. Some of these disabilities may be remedied by term lending institutions; others may require legislative action like conversion of concerns into corporate bodies which normally facilitate flow of funds and assure continuity of operation. But even such steps cannot deal with the fact that certain industries, the demand for whose products increases faster than that of others as per capita incomes increase, must experience

a higher growth rate than the latter. Some valuable evidence on this point is available from the periodical studies conducted by the Reserve Bank of India on the finances of joint stock companies.

[(*a*) Finances of Joint Stock Companies, 1960, (R.B.I. Bulletin, June, 1962) covering 1001 such companies, each with paid-up capital of over Rs. 5 lakhs.

(*b*) Finances of small Public Limited Companies, 1960, (Bulletin, October, 1962) covering 1017 such companies, each with paid-up capital of Rs. 5 lakhs and below, and

(*c*) Finances of Private Limited Companies, 1960, (Bulletin, December, 1962) covering 333 such companies, each with paid-up capital of Rs. 5 lakhs and over.

The methodology, etc. of these studies have been explained in the Bulletin.]

V.30. These classes of companies do not exhaust the range catered to by SFCs, which includes also proprietary and partnership concerns and even co-operatives. But the findings of these studies are broadly applicable to the experience of these Corporations and contain some useful lessons.

V.31. These studies reveal clearly that the food and textile groups of industries to which SFCs have, with a few exceptions, generally diverted a good part of their resources, are not the groups where capital formation was proceeding apace. The latter groups—in the 1001 company study—were: transport equipment; electrical machinery, apparatus, appliances, etc; machinery (other than transport and electrical); basic industrial chemicals; medicines and pharmaceutical preparations; and paper and paper products. In the sector of small public companies and of the private companies studied by the Reserve Bank too, the picture is broadly the same.

V.32. A comparison with the industry-wise distribution of assistance sanctioned by ICICI—which has not the drawbacks of SFCs—upto 1962 is revealing. The major groups are: iron and steel, 15.6%; chemicals and chemical products, 13.6%; electrical equipment, 9.9%; machinery manufacture other than electrical, 9.9%; paper and pulp, 8.9%; automobiles and cycles, 7.6%; glass, pottery, etc., 5.1% and electricity, gas and steam, 5.0%. The distribution of loans approved by IFC upto June, 1962 is as follows: food, except beverage, 29.2%; basic industrial chemicals including fertilizers, 11.6%; textiles, 10.8%; paper and paper products, 10.3% and cement, 5.8%.

V.33. Apart from the selection of industries to be financed, the ceiling on the size of individual loans by SFCs (Rs. 10 lakhs upto April, 1962, relaxed to Rs. 20 lakhs thereafter for public limited companies and co-operatives) may also have handicapped their own business by concentrating on small and medium-sized concerns. Reserve Bank studies indicate that during 1956 to 1960, the average rates of capital formation in the public limited companies were uniformly above those in the

private companies, the average size of the latter being about a third of the former. This holds for all the seven different indices, viz., gross and net fixed assets and capital formation (4), gross and net total assets formation (2) and inventory accumulation. There is evidence that since April, 1962, SFCs have, taking advantage of the amendment, sanctioned sizable amounts to relatively larger-sized concerns. This is as it should be as the Corporations by increasing their turnover more than proportionately to the administrative cost will be able to attain a position of viability earlier than before and will thereby be able to serve better the needs of small and "non-traditional" industries than they are doing at present.

Grant of loans for working capital

V.34. When the question of providing working capital loans was considered at the SFCs' Conferences of 1954 and 1955, it was held that while there should be no objection to granting such loans in appropriate cases, there should be no overlapping of functions between SFCs and commercial banks. SFCs normally provide working capital only in appropriate cases e.g., where it is not forthcoming from banks, etc., the unit concerned is well-organised and counts in the economy of the State, and its products command a ready market. The Second SFCs' Conference of 1955 evolved a formula for such loans on the premise that well-managed and financially sound concerns did not experience much difficulty in obtaining working capital from banks, and that normally there should be no competition with banks. It laid down that where the loan from SFCs was primarily for block capital, the working capital constituent should not exceed 25% of the total amount applied for; loans primarily for working capital could be given *only* if the concern failed to obtain it from banks.

V.35. Since then the situation has changed much. In the context of continuing pressure of demand for bank advances from all sectors, the assumption that working capital loans from SFCs would mean encroachment in the business of banks has lost much significance. Also, as the supply of many industrial raw materials has been uncertain from time to time, manufacturers have often to hold larger stocks to ensure fuller utilisation of capacity. At the same time, higher prices make it difficult to finance such inventories. So the provision of relatively longer term working capital is now more important, especially for newly set-up units. Accordingly, the Eighth SFCs' Conference of 1961 laid down the following general principles, leaving it to the Corporations to adjust them where necessary.

I. Considerations for the grant of working capital loans:

(*a*) The goods manufactured by the concern are of standard quality and have a ready market which is not temporary or transient.

(*b*) For a new concern, initial working capital is required to hold the necessary minimum level of raw materials, stores and finished goods.

(*c*) The unit belongs to a category of high priority or importance from the point of view of industrial development in the State.

(*d*) It is partly lying idle for lack of working capital.

(*e*) The loan is required to provide margin for accommodation from banks against raw materials and finished goods.

(*f*) The nature of industry is such that short term finance granted by banks is not suitable and the working capital is needed for a period of at least 2 to 3 years.

II. Conditions subject to which loans for working capital may be sanctioned:

(*a*) The loans should be secured primarily against block assets, and should not be of the nature of cash credit arrangements.

(*b*) When the loan is required for working capital in combination with block capital, the portion of working capital should not ordinarily exceed 50% of the total amount of the loan.

(*c*) Loans primarily for working capital should not ordinarily be for periods exceeding 5 years.

(*d*) The loans should not be such as to encourage overtrading.

V.36. We show below the Statewise details of loans with working capital component sanctioned by SFCs during 1961-62 and the actual working capital component therein:

(Rs. lakhs)

Corporation of	Loans to small units		Loans to others		Working capital component of (2) Amount	Working capital component of (4) Amount
	No.	Amount	No.	Amount		
	(1)	(2)	(3)	(4)	(5)	(6)
1. Andhra Pradesh	8	4.25	1	2.00	1.80	0.45
2. Assam	3	1.26	—	—	0.18	—
3. Bihar	—	—	—	—	—	—
4. Gujarat	16	9.46	6	26.00	6.55	12.94
5. Jammu & Kashmir	—	—	—	—	—	—
6. Kerala	3	3.23	[illegible]	24.00	0.80	2.05
7. Madhya Pradesh	26	18.61	2	12.00	10.84	7.00
8. Maharashtra	53	14.38	1	1.00	8.56	0.30
9. Mysore	27	14.19	2	16.00	6.60	3.50
10. Orissa	1	0.26	—	—	0.06	—
11. Punjab	—	—	—	—	—	—
12. Rajasthan	1	0.40	1	1.00	0.10	0.40
13. Uttar Pradesh	1	1.20	—	—	0.28	—
14. West Bengal	1	1.60	—	—	0.68	—
Total	140	68.84	[illegible]	82.00	36.45	26.64

(Rs. lakhs)

	Total of loans with working capital	Working capital portion in (1)	% of (2) to (1)	All sanctions i.e. including loans with *no* working capital component	% of (2) to (4)
	(1)	(2)	(3)	(4)	(5)
Small	68.84	36.45	53%	429.90	8.5%
Others	82.00	26.64	32%	720.36	3.7%
	150.84	63.09	42%	1150.26	5.5%

V.37. Kerala SFC, it may be stated, raises the proportion of working capital component in suitable cases to 50%, while Madhya Pradesh SFC had sanctioned loans amounting to Rs. 6.59 lakhs for working capital *only*. The above data show that out of the total sanctions with working capital component amounting to Rs. 150.84 lakhs in 1961-62, the working capital component was Rs. 63.09 lakhs i.e. about 42%. But it will be seen that in relation to *total* loans sanctioned in 1961-62, the percentages of loans granted for working capital purposes to small and other units work out to only 8.5 and 3.7 respectively. This is explained by the fact that the provision of such loans is outside the sphere of the normal activities of SFCs. Sometimes, the units are advised to contact commercial banks for the purpose. It is also the experience of SFCs that in many deserving cases such loans could not be granted due to lack of adequate security.

V.38. Further, new industrial concerns which *propose to engage* themselves in manufacture, etc. were made eligible for financial assistance from SFCs only after Sec. 2(*c*) of the SFCs Act was amended in 1955. Even by 1961-62, not many SFCs entertained freely applications from newly set-up concerns, perhaps because the appraisal of such applications is often more difficult in the absence of the record of past performance. But such concerns are more in need of working capital loans, which they may not be able to obtain from normal banking channels, as compared with the older, established concerns with banking arrangements. It would thus appear that the quantum of working capital supplied by SFCs is not meagre. It may further increase with the widening of the scope of operations of SFCs after the amendment of Sec. 2(*c*), referred to earlier, making the hotel and transport industries and industrial concerns engaged or to be engaged in the development of industrial estates also eligible for assistance.

V.39. In reply to the questionnaire issued by this Working Group, all SFCs except that of West Bengal have stated that there is a demand for working capital along with block capital loans. Most SFCs give as working capital either 25% of the block capital or an amount equal to the estimated working capital requirements for two to three months. Uttar Pradesh SFC usually sanctions upto 20% of the total loan as

working capital; no assessment is made of requirements for specified periods. The question whether units have suffered for want of working capital has been answered by eight SFCs in the affirmative and five in the negative. Most SFCs had no particular suggestions for modification of their present practices.

V.40. In answer to the question whether it would be more convenient to obtain both equipment and working capital loans from SFCs, the consensus of opinion of Chambers of Commerce, Associations, etc. was that it would be advantageous to do so. In case SFCs could not provide both equipment and working capital loans, it has been suggested by some that they might guarantee loans obtained for working capital from banks. However, we consider that, as a rule, working capital should be obtained from commercial banks, and SFCs might provide the permanent or initial working capital which is included in the cost of the project.

Present position regarding loans on an agency basis—States, terms, amounts, industries and problems

V.41. Under Sec. 25(1)(*d*) of the Act, a SFC may act as agent of the Central Government, State Government, IFC or any other financial institution notified in this behalf by the Central Government, in the transaction of any business with an industrial concern in respect of loans or advances granted, or debentures subscribed, by any one of them. The provision was introduced in 1956, after the Second SFCs' Conference in 1955. It was then recognised that, following the policy announced by the Central Government, under the State Aid to Industries Act/Rules, substantial Government loans would be made available to small scale industrial units on liberal terms, such as low rate of interest and low margin on security, but that this was likely to impinge on the SFCs' field of operations. So a modus vivendi had to be evolved to protect SFCs' interests and also make a beginning of institutionalising the flow of such Government funds to small ventures. The Conference recommended amending the Act to authorise SFCs to function as agents of State Governments to scrutinise and sanction loan applications received by latter from small enterprises, to disburse such loans, and to collect and remit the amounts to Governments.

V.42. So far, SFCs in nine States, viz., Andhra Pradesh, Maharashtra, Uttar Pradesh, Punjab, Kerala, Rajasthan, Assam, Gujarat and Orissa have been appointed as agents of their respective State Governments for channelling block loans to small units under the State Aid to Industries Act/Rules, as the case may be. The Government of Madhya Pradesh had agreed to channel these loans through the SFC, but so far no action has been taken in the matter. Though West Bengal Corporation was also so appointed, the arrangement has not been implemented as the Accountant General, West Bengal, has been reported to have raised certain constitutional and statutory objections to it. The Government

of Bihar have recently agreed to appoint Bihar SFC as their agent. The question was under consideration in the remaining States (viz., Jammu & Kashmir and Mysore). The Government of Madras have decided not to appoint MIIC as their agent. Loans disbursed under agency arrangements are not shown in the balance sheet of any SFC except that of Punjab. All SFCs may in future show these loans in the balance sheet, together with the amounts outstanding to State Governments on their account.

V.43. The terms of such agency differ from State to State. Thus:—

(1) *Uttar Pradesh* : The SFC handles loans between Rs. 15,000 and Rs. 1 lakh. So far, a sum of Rs. 1.69 crores has been placed at its disposal. The rate of interest to borrowers varies with the amount of loans sanctioned as under:

Loans between Rs. 15,000 and Rs. 25,000	3%
Loans between Rs. 25,001 and Rs. 50,000	4%
Loans exceeding Rs. 50,000	5%

Commission at 2% on the amount disbursed during a particular year is allowed to the SFC as administrative charges.

(2) *Andhra Pradesh :* The SFC is authorised to disburse and recover loans sanctioned by the State Government. It does not sanction loans on behalf of the latter. The rate of interest to borrowers is 2½% for industrial co-operatives and 3% for others. The SFC gets 2% commission on amounts disbursed. Disbursements during 1959-62 totalled Rs. 14.47 lakhs.

(3) *Kerala :* The SFC has been empowered to sanction and disburse loans between Rs. 10,000 and Rs. 1 lakh to approved industries in the small scale sector, other than industrial co-operatives at 3½% upto Rs. 50,000 and 5½% above that limit. A sum of Rs. 22 lakhs was placed at its disposal during the period 1960-62.

(4) *Rajasthan :* The SFC is authorised to grant loans of over Rs. 10,000 and upto Rs. 50,000. Rs. 6.10 lakhs have been allotted by Government for the purpose. The rate of interest varies with the capital employed in the industry as under:

Capital upto Rs. 2 lakhs	3%
Capital above Rs. 2 lakhs and upto Rs. 4 lakhs	4½%
Capital above Rs. 4 lakhs	6%
Industrial co-operatives pay a flat rate of	2½%

(5) *Punjab :* The limits between which the SFC operates are Rs. 25,000 and Rs. 50,000. The State Government have placed Rs. 40.50 lakhs at the disposal of the SFC. For industrial co-operatives, the rate of interest is 2½%. For others, the rate varies: loans upto Rs. 25,000, 3%; loans exceeding Rs. 25,000, 5½%.

(6) *Assam :* The SFC can sanction and disburse loans exceeding Rs. 10,000. It has not so far disbursed any amount as the agreement has

not yet been finalised. For individuals and institutions, the rate of interest is 3% and for industrial co-operatives, it is 2½%.

(7) *Gujarat :* The SFC has been acting as agent since August, 1960 for loans to small industrial units of between Rs. 10,000 and Rs. 75,000, and, in exceptional cases, upto Rs. 1 lakh. Since January, 1962, it can sanction and disburse loans exceeding Rs. 10,000 and upto Rs. 25,000 at 4% interest, and keeping a margin of 25%. A sum of Rs. 16.50 lakhs has so far been earmarked by the State Government for the purpose.

(8) *Maharashtra :* The SFC can sanction and disburse loans ranging from Rs. 10,000 to Rs. 75,000, and, in exceptional cases, upto Rs. 1 lakh to parties other than industrial co-operatives. The arrangement has been modified from time to time. Since March, 1961, under instructions from Government, the SFC is lending its own funds to small units on liberalised terms under the State Aid to Industries Rules; Government have extended full guarantee for such loans for a period of 10 years. So far, they have given guarantee to the extent of Rs. 30 lakhs in 1960-61, Rs. 60 lakhs in 1961-62, Rs. 50 lakhs in 1962-63, and Rs. 75 lakhs in 1963-64. The rates of interest on loans disbursed under the liberalised scheme are:—loans exceeding Rs. 10,000 and upto Rs. 25,000, 4½%; loans exceeding Rs. 25,000 and upto Rs. 50,000, 5½% to 7% (lower rates being charged to units situated in industrially backward areas); loans exceeding Rs. 50,000 and upto Rs. 1,00,000, 7% (being the Corporation's current lending rate). The difference between the Corporation's normal lending rate and concessional rate is subsidised by the State Government.

In February, 1962, the State directed the SFC to disburse from out of its own funds, loans which had already been scrutinised and processed by the Director of Industries for amounts exceeding Rs. 3,000 but not exceeding Rs. 10,000 at a concessional rate of interest of 3%, Government subsidising the Corporation to the extent of the difference between its current lending rate and the actual rate charged to the concern. But no disbursement was made under this arrangement. It is understood that the loans in question have been passed on to a commercial bank for disbursement.

(9) *Orissa :* The SFC is authorised to sanction loans for amounts ranging between Rs. 20,000 and Rs. 25,000, for which Government have placed a sum of Rs. 2.25 lakhs at its disposal. The prescribed rate is 6% with a rebate of 50 nP. per cent for prompt payment of interest and repayment of principal.

V.44. Under the Government of India's liberalised scheme of financial assistance to small units, it is provided that SFCs would be entitled to a margin of not more than 2% for handling these loans on behalf of Government; this margin is to be borne equally by the Central and State Governments. On this basis, States have been giving SFCs a 2% commission for handling these loans, the commission payable being calculated on the amount disbursed in any one year and not on the amount outstanding. Thus, a mere 2% on each loan in the first year

alone is expected to cover the administrative costs of the SFC over the entire life of the loan. The only exception is Maharashtra where, for loans out of funds provided by the State, the SFC gets commission on the basis of the amount outstanding—subject to a maximum commission of Rs. 50,000 in any one year, and where the SFC also gets an annual subsidy of Rs. 10,000 for administrative expenses. It is suggested that to make it worthwhile for the Corporations to undertake agency functions, commission should be paid on the same basis as in Maharashtra. Even for the normal loans of SFCs which are of consideraby larger size than the agency loans, the margin of about 2% which is now available to them is not considered adequate.

V.45. The attention of the Group has also been drawn to the fact that payment of agency commission due to SFCs is often kept in arrears. Thus, while no commission has so far been paid to the SFC, it has had to pay income tax on the amount yet to be received from the State Government. State Governments may, therefore, ensure that agency commission is paid to SFCs promptly, as and when due.

V.46. The agency system, as pointed out earlier, is being worked differently in different States. Apart from this, Andhra Pradesh SFC is not authorised to sanction loans but only disburses and recovers loans granted by the State. The Seventh SFCs' Conference, 1960, it may be recalled, had observed that this procedure was not in accord with the ultimate objective of the agency arrangement, viz., to institutionalise credit to small industrial units in due course; but the position continues as before.

V.47. Table XI shows the loans sanctioned, disbursed, etc. by six SFCs as agents of the States as on 31st March, 1961, 1962 and 1963. The average value of sanctions was only Rs. 0.4 lakh in 1962-63. In Rajasthan and Gujarat, it was only Rs. 0.15 lakh. As the full amount sanctioned by SFCs is often not drawn by all borrowers, the average value of disbursements in different States would be even smaller.

V.48. The Small Scale Industries Board, at its 9th meeting in September, 1957, had recommended that to progressively bring SFCs into the sphere of financing small scale industrial units, at least 10% of block loans given by the State Governments to such units should be routed through SFCs. This would also improve the latter's finances and partly help to reduce the subventions which the States are having to pay to meet the deficit in SFCs' net profits in relation to the guaranteed dividends.

V.49. While sanctioning loans to small units out of their own resources and on their own terms, SFCs generally follow a practice of not entertaining applications from such units upto certain limits e.g., Rs. 75,000 in the case of Maharashtra, Rs. 25,000 in the case of West Bengal and Rs. 10,000 in Kerala. This is to avoid overlapping as loans upto these limits are to be given by the State Departments of Industries. The Seventh SFCs' Conference also held that while it would not be

TABLE XI

Particulars of SFCs' loans and advances under Agency Arrangement with State Governments

(Rs. '000)

Corporation of	Applications received						Applications sanctioned						Amount disbursed			Cumulative		
																Sanctions		Out-standings
	1960-61		1961-62		1962-63		1960-61		1961-62		1962-63		1960-61	1961-62	1962-63	As on 31-3-1963		
	No.	Amount	No.	Amount	No.	Amount	No.	Amount	No.	Amount	No.	Amount	Amount	Amount	Amount	No.	Amount	Amount
1. Andhra Pradesh	N.A.		N.A.		N.A.		N.A,		N.A		N.A.		710(a)	159(a)	180	N.A.		N.A.
2. Gujarat	151	5768	77	2749	22	491	45	1448	39	955	8	126	399	853	409	92	2529	2225(b)
Average		38.2		35.7		22.3		32.1		24.5		15.8					27.5	
3. Kerala	108	5358	46	2392	34	1889	40	1648	52	2133	22	1002	695	1260	1099	97(c)	4024(c)	2905
Average		49.6		52.0		55.6		41.2		41.0		45.5					41.5	
4. Maharashtra	256	12334	317	14824	265	13126	85	3634	138	5254	114	4747	1772	411 3277(d)	88 4078(d)	478	19352	2312 7204(d)
Average		48.2		46.8		49.5		42.7		38.1		41.6					40.4	
5. Punjab	54	2316	60	2665	97	3843	28	1040	35	1495	32	1269	728	926	906	118	4709	2655
Average		42.9		44.4		39.6		37.1		42.6		39.6					39.9	
6. Rajasthan	43	859	34	785	18	615	23	334	13	208	5	75	158	219	63	41	617	[illegible]
Average		20.0		23.1		34.2		14.5		16.0		15.0					15.3	
7. Uttar Pradesh	98	5782	75	4647	68 12(f)	4293 1315(f)	81	3902	42	2437	41 5(f)	2027 305(f)	2004	1464	1361	333(e) 5(e)(f)	13576(e) 305(e)(f)	7039
Average		59.0		62.0		70.1		48.1		58.0		50.7					41.1	
Total (excluding Andhra Pradesh)	710	32417	609	28062	516	25572	302	12006	219	12482	227	9551	5756	8410	8004	1164	45112	24732
Average		45.7		46.1		49.6		39.8		57.0		42.1					38.8	

(a) Includes disbursement under State Governments special scheme to ameliorate unemployment situation in Hyderabad and Secunderabad.
(b) Includes Rs. 12,01,346 being outsandings of loans disbursed before they were transferred to the Corporation.
(c) After adjustment for "cancelled" sanctions.
(d) Corporation's funds.
(e) Effective sanctions.
(f) These relate to loans for "Cold Storage" under the Agriculture Department Scheme.

economical for SFCs to handle loans below a certain amount (say Rs. 5,000 or Rs. 10,000 depending upon the requirements of individual States), duplication should be avoided, and all loans within a specified range should be routed through SFCs. Also, since agency loans carry subsidised rates of interest, SFCs cannot disburse them within the specified limits out of their own funds; the higher rates of interest of these institutions would not attract small borrowers. Keeping these variations in mind, the Committee on Credit Facilities of the Small Scale Industries Board (SSIB), at its 6th meeting held in Calcutta in January, 1961, held that the procedures and agency arrangements should be standardized. It recommended that the States might ordinarily grant loans upto Rs. 15,000, and SFCs should act as the agents of Government for higher amounts in all cases. Where, however, the States were already permitting SFCs to grant smaller loans, they might continue to do so.

V.50. The Development Commissioner, Small Scale Industries, stated in a note submitted for consideration of the Ninth SFCs' Conference, 1963, that the expectation that SFCs would be able to function effectively as credit institutions to small units has not been realised to any appreciable extent. Some States do not have adequate funds to meet the demand for such small loans. At the 20th meeting of the SSIB in April, 1962, it was recommended that, as in Maharashtra, States which did not have adequate funds should arrange with their SFCs to advance loans out of the latter's funds on liberalised terms regarding interest, margin, etc. against State Government's guarantee and subsidy. This recommendation was sent to all the States but no action has yet been taken. It is not known how far this is due to the unwillingness of the States to guarantee such loans, and to bear the subsidy for interest which will be more than the 2% now given to SFCs for handling loans out of Government funds, even if the Central Government meet a part of the excess over 2%. SFCs may not, however, be very enthusiastic to undertake this business now as many of them are acutely short of funds to meet the demands of medium, and to some extent small-sized, units.

V.51. The two major instances where development banks abroad are known to perform such agency functions are the business of the Industrial and Mining Development Bank of Iran with "Managed Funds", and of the Industrial Development Bank of Turkey out of the Marshall Plan Private Enterprise Fund. In both these cases, the agency terms with the governments are much more attractive to the banks than in India, especially if it is considered that, for these agency loans, these two banks are not restricted, unlike in India, to loans to very small enterprises. After the former bank was set up, the Government of Iran, in addition to giving it an interest-free advance of Rials 600 mn., transferred to it the management of certain loan portfolios of the Bank Melli Iran and the Industrial Credit Bank (both State-owned) totalling some Rials 1,400 mn. (or Rs. 84 mn. at the rate of Rial 1 = Re. 0.06). The transfer of such a large portfolio by Government afforded, according

to the bank, the most effective assistance to its operations in the early stages. It provided the bank with a source of immediate income without assuming any risk of loss on the loans it administered as agents, and also invaluable opportunities to gain experience of many problems of industry—management, marketing, finance, etc.

V.52. The agreement with Government provides that repayments received from borrowers of the Managed Fund are to be repaid to the two transferor banks not immediately, but in 14 approximately equal semi-annual instalments, commencing after 8 years from the date of the agreement with Government, viz., 8th November, 1959. For the period that such repayments are at its disposal, it will charge an *annual* commission fee of 3% on loans made from such Fund, except that no fee shall be charged on loans where payment of principal or interest is in default. Repayments are to be re-lent for the same purposes for which its other funds are lent. This is ensured by the provision in the Agency Agreement that Managed Funds shall be granted a pro rata participation in each such loan of the bank.

V.53. In Turkey, the Marshall Plan Private Enterprise Fund was set up under an agreement in 1951, between the Turkish Government and the Special Mission to Turkey of the USA Economic Co-operation Organisation. The Industrial Development Bank administers the Fund, for a management fee of 4% per annum of loans outstanding from the Fund, to give term loans to fully private owned industrial units for purposes which fall within its statute. By the end of 1961, loans allocated from the Fund and outstanding amounted to TL 214 mn. and TL 113 mn. respectively, forming as much as 48% and 52% respectively of all the loans of the bank. Also the Fund loans fetch a 4% margin against the 3% it earns on its other loans, and any losses arising out of the former are debitable to the Fund and do not affect the finances of the bank.

V.54. In addition to acting as agents of State Governments, under Sec. 25(1) (*d*) of the Act, SFCs can also, as stated in the beginning of this Section, act as agents of financial institutions to be notified in this behalf by the Central Government. In June, 1962, the Central Government notified ICICI as a financial institution for the purpose of this Section. But so far such agency functions with other institutions have not developed. Since ICICI does not have branches in other parts of India, it could consider appointing SFCs as its agents for loans given to industrial concerns situated in distant parts of the country. In particular, SFCs could undertake periodical inspections of borrower concerns on its behalf.

Loans and advances by State Financial Corporations in participation with other financial institutions

V.55. SFCs can also finance industrial concerns in participation with other lenders. So far this has made very little progress for various

reasons. Participation presupposes a measure of comparability among the participants in such matters as technical skill in appraisal. For a number of SFCs set up in recent years, this condition was not satisfied vis-a-vis institutions like IFC and ICICI. Also it was only in April, 1962, that the SFCs Act was amended to increase the total assistance to a public limited company and a co-operative society to Rs. 20 lakhs from Rs. 10 lakhs till then. This has brought into the ambit of SFCs relatively larger-sized concerns where participation is more likely to arise.

V.56. The Seminar on Financing of Small Scale Industries in India (Hyderabad, 1959), suggested evolving agency arrangements between commercial banks on the one hand and SFCs on the other, or participation in the extension of loans between SFCs and commercial or co-operative banks, etc. (*i*) to reduce the risks of term lending and (*ii*) to overcome 'borrower-resistance' by enabling them to approach only one institution for their short as well as long term requirements. The Scheme for Guarantee of advances granted to small scale industries also envisages participation arrangements between the banks inter se as well as between banks and other specified credit institutions. The question of SFCs financing industrial concerns jointly with other agencies was considered at the Sixth and Seventh SFCs' Conferences. It was thought that the appointment of banks as agents of SFCs would eventually pave the way for working out participation loan arrangements and that there was no use forcing the pace of development. Seven SFCs, viz., those of Maharashtra, Andhra Pradesh, Punjab, Uttar Pradesh, West Bengal, Rajasthan and Orissa have appointed the State Bank of India as their agent to disseminate information regarding their activities, forwarding to them loan applications received from mofussil parties, furnishing credit information on prospective borrowers, disbursing loans, etc. SFCs in Maharashtra, Andhra Pradesh and Madhya Pradesh have also appointed certain other scheduled banks as their agents for these purposes.

V.57. Participation arrangements may be worked out in conjunction with other institutions in the matter of extension and guarantee of loans and underwriting of issues of shares and debentures. However, Table XII (page 118) will show that SFCs have made little progress in the field of joint lending. Upto 6th February, 1963, Maharashtra, Gujarat and West Bengal SFCs have lent jointly with ICICI in two, one and two cases respectively, generally taking a first legal mortgage pari passu with ICICI. MIIC has entered into joint underwriting operations with ICICI in four cases, and direct subscription to shares in one case.

V.58. Bihar SFC has also participated in one case with IFC; these institutions have sanctioned Rs. 10 lakhs and Rs. 20 lakhs respectively to a paper mill in Bihar in 1960-61 against mortgage of fixed assets on a pari passu basis. Rajasthan SFC has made arrangements with IFC for participation loans to public limited industrial

concerns in the State. It will finance a unit upto Rs. 20 lakhs, and loan amount above Rs. 20 lakhs will be financed by IFC on a pari passu charge basis. SFCs in Bihar, Gujarat, Madhya Pradesh and Uttar Pradesh hold that there are good prospects for participation loans, while Assam, Jammu & Kashmir and Punjab SFCs hold that there are not much prospects for participation loans. SFCs in Andhra Pradesh, Maharashtra, Rajasthan, Uttar Pradesh and West Bengal hold that in the case of participation loans, SFCs should have pari passu charge. Orissa Corporation is of the view that in case of participation with IFC and ICICI, SFCs should have pari passu charge but with commercial banks a first charge. Mysore SFC feels that participation loans with commercial banks are not feasible; with IFC they are useful and advantageous.

V.59. The question of participation loans has gained importance in the context of some of the recent amendments to the SFCs Act, extending the sphere of co-ordination between various institutional agencies and SFCs, and other developments like commercial banks stepping into the domain of formal term lending to industries, setting up of SIDCs in some States, etc. Under the recent amendments to their statute, SFCs can undertake a few new items of business, some involving relatively large investments e.g., the financing of transport industry or industrial estates which might require outlays beyond the statutory provisions of these institutions to accommodate. A number of industries has also been scheduled for development in the private sector under the Third Five Year Plan and there is likely to be increasing demand for industrial finance. With the impact of developmental expenditure, the cost of putting up a project is also rising, emphasising the need for participation loans to reduce risks. Further, in view of statutory and other limitations, any one institution such as a SFC may not be able to meet singly all the credit needs of an industrial concern. Apart from loan capital, the demand for equity capital too is likely to be large. While SFCs cannot as yet directly participate in equity shares, they can assist concerns by underwriting issues. Thus, SFCs must work in close co-operation with other experienced financial institutions. They are also likely to benefit much from their association with institutions like ICICI and IFC in the important matter of appraisal of loan applications. The extent and manner in which SFCs may collaborate with other agencies for granting loans is indicated below, as submitted to the Ninth SFCs' Conference.

(*a*) A medium-sized unit organised as a public limited company or co-operative society whose requirements exceed Rs. 20 lakhs, which is the statutory limit for advances to such a concern by SFCs, may be financed jointly with IFC/ICICI. The SFC may continue to service the loan account, act as agent of IFC/ICICI to the extent of the additional loan [this is permissible under Section 25(1)(*d*) of the Act] and accept a pari passu charge on the security which may continue to be supervised by it. This will mutually benefit all the parties. If the industrial unit is a proprietary or partnership concern or a private limited

TABLE XII

Joint lending/financing by State Financial Corporations, Madras Industrial Investment Corporation Ltd. and the Industrial Credit and Investment Corporation of India Ltd.

(Amount in Rs. lakhs)

Name of institutions	Year	Assistance by ICICI	Assistance by SFC	Security for ICICI	Security for SFC	Remarks
(1)	(2)	(3)	(4)	(5)	(6)	(7)
Maharashtra State Financial Corporation (MSFC)						
Unit No. 1	1961	F.E. 4.05	1958 R.L. 3.00	First legal mortgage pari passu with MSFC	First legal mortgage pari passu with ICICI	The processing was done at two different times.
Unit No. 2	1962	F.E. 5.12 R.L. 5.00	1955-57 R.L. 5.87	-do-	-do-	-do-
Gujarat State Financial Corporation (GSFC)						
Unit No. 1	1961	F.E. 10.00 U.W. 5.00	1961 R.L. 10.00	First legal mortgage pari passu with GSFC	First legal mortgage pari passu with ICICI	The processing was done independently by the two institutions.
West Bengal Financial Corporation						
Unit No. 1	1962	U.W. 7.00	1956 R.L. 5.00 1961 R.L. 5.00 1962 U.W. 5.00	—	First legal mortgage guaranteed by two directors of the Company	This is a case of underwriting by the two institutions.

Unit No. 2	1960	R.L.	20.00	1958	R.L.	1.50	First legal mortgage on Thana block assets and second charge on Calcutta block assets	First legal mortgage on Company's property in Calcutta	The operations took place at different points of time, and the security for each institution was independent.
Madras Industrial Investment Corporation (MIIC)									
Unit No. 1	1960 1962	R.L. R.L.	35.00 7.50	1960	U.W.	15.00	First legal mortgage debentures jointly with Bank of India	—	In these cases, the kinds of assistance provided by Madras Industrial Investment Corporation and Industrial Credit and Investment Corporation of India are different. However, generally an exchange of information takes place between the two institutions.
Unit No. 2	1962	F.E. R.L.	15.00 5.00	1962	U.W.	10.00	First legal mortgage	—	
Unit No. 3	1961 1962	F.E. F.E.	27.13 3.62	1961	U.W.	15.00	First legal mortgage	—	
Unit No. 4	1962	F.E.	64.26	1962	U.W.	20.00	First legal mortgage	—	
Unit No. 5	1960	R.L.	50.00	1960	D.S.	100.00	First legal mortgage	—	

F.E. = Foreign Exchange loan
R.L. = Rupee loan

U.W. = Underwriting of shares
D.S. = Direct Subscription to shares.

company, for which the limit of advance by the SFC is Rs. 10 lakhs, such an arrangement can be made only with ICICI as IFC cannot finance such a concern.

(*b*) Where a concern requires assistance both in foreign currency and in rupees, former may be provided by IFC/ICICI depending upon the form of organisation of the concern; SFC may provide the rupee loan, both agencies having pari passu charge on the securities.

(*c*) Commercial banks and SFCs may jointly finance an industrial concern, against composite security for acquiring block assets as well as for working capital purposes, banks taking the earlier maturities (as they do not normally finance long term loans)—for which they can also obtain refinance from RCI—and SFCs the later ones.

V.60. In participation loans, the co-operating institutions generally enter into a formal agreement providing for the share of each participant, the distribution of income and expenses, the duration of the agreement, the mode of administration, etc. The method of administration differs with the needs of each case. The facilities to the borrower may be provided by one of the participating institutions which may act as agent for the rest and keep the security documents, disburse the loan, receive repayments and undertake all related work; or, each participant may fulfil its obligations direct to the customer. The loan agreement with the borrower may usefully contain certain clauses which spell out the agent's functions vis-a-vis the other participating institutions. In the event of the borrower's failure to implement the terms of the contract, it should not be difficult for the concerned institutions to agree to a conjoint action consistent with the interests of all the participants.

V.61. There is also scope for commercial banks to act as agents of SFCs where latter have no branches. Apart from being mutually beneficial, it will increase the scope of business of the Corporations and publicise their activities in mofussil areas.

V.62. Nevertheless, the scope for participation in loans will, and also should, be somewhat limited. Financing institutions have their own independent methods of scrutiny and also their own separate entities to maintain. Collaboration among equals holds more promise than among such unequal partners as SFCs on the one hand and IFC/ICICI on the other; and they are likely to remain so for many years. Also, it must be stressed that the main function of SFCs is to finance medium and small scale industrial units; this should absorb all their energies and resources. Excess emphasis on securing business in participation with other agencies will make them lean more towards financing larger borrowers, to the detriment of attention being given to medium and small units. But participation will have three benefits: the cost of appraisal will be less—being shared by the participants, it will gradually improve SFCs' ability to appraise loan applications through contact with the better organized financing institutions, and it will enable them to entertain applications with a foreign exchange component if exchange is

provided by the participants. But SFCs would have greater manoeuvrability if the Government were to make periodical allotments of exchange to them, for financing the foreign exchange cost of projects falling within any defined body of priorities that Government may lay down.

Business other than that of loans and advances

V.63. In addition to their main function of granting loans, SFCs may also undertake a few other kinds of business:—(*i*) Guaranteeing of loans raised by industrial concerns, (*ii*) guaranteeing of deferred payments, (*iii*) subscribing to debentures of an industrial concern, repayable within 20 years from the date of subscription, and (*iv*) underwriting issues of stock, shares, bonds and debentures by industrial concerns. Except (*iv*), assistance under (*i*), (*ii*) and (*iii*) must, under Sec. 25(2), be sufficiently secured by pledge, mortgage, etc. of assets or guaranteed, as in the case of loans and advances under Sec. 25(1)(*g*). These activities are now considered.

(*i*) Guaranteeing of loans

V.64. Under Sec. 25(1)(*a*) of the Act, a SFC may guarantee: (*a*) loans raised by industrial concerns which are repayable within a period not exceeding 20 years and are floated in the public market (provision in force since 1st August, 1952); and (*b*) loans raised by industrial concerns from scheduled banks or State co-operative banks (provision introduced on 16th April, 1962). Provision (*a*) enables it to guarantee loans raised by an industrial concern in the public market. The word 'loans' would generally mean debentures floated in the open market. During the discussion in Parliament in 1951 on this provision, a suggestion was made to drop the words "and are floated in the public market" as not to preclude SFCs from guaranteeing loans raised by private arrangement. Shri C. D. Deshmukh (then Finance Minister) did not accept this; he thought that there should be the touchstone of the public market on loans which SFCs may guarantee. He further averred that these words were inserted in the clause in the interests of conservative finance. His submission was that there was nothing to stop a loan about which there might be a private arrangement, from being floated in the market. Thus, the intention of the legislature was that SFCs may only guarantee loans raised in the market. As yet, no SFC has guaranteed such a loan.

V.65. Provision (*b*) was introduced for special types of joint lending by SFCs and other institutions e.g., where concerns find it difficult to get working capital funds from sources other than SFCs, like banks, etc., which may consider the residuary security left for covering their advances to such concerns as being inadequate—in size or quality—to cover their risks after SFCs had obtained a charge on their other, major, assets for financing the acquisition of fixed assets. Tea gardens present such an instance. Normally, because of the natural hazards to which a tea garden is exposed, commercial banks secure their short term advances to gardens

with the fixed assets in addition to a hypothecation of the crop. If the garden obtains a term loan from a SFC, the bank would tend to be deprived of the fixed assets as a backing for its working capital loan when a guarantee may induce it to continue its finance without a charge on the fixed assets.

V.66. To ensure that a SFC does not enter into large commitments in the form of guarantees, or in underwriting shares, the Act has limited the aggregate of such contingent liabilities to twice its paid-up capital and reserve fund; it may be stretched to three times, with the prior approval of the State Government and in consultation with Reserve Bank. Besides, the Act has placed an overall limit to the total amount outstanding in respect of any industrial concern in the form of assistance by way of loans, guarantees, etc. at Rs. 20 lakhs in the case of public limited companies and co-operative societies and Rs. 10 lakhs in other cases.

(*ii*) Guaranteeing of deferred payments in respect of capital goods purchased in India

V.67. In terms of Sec. 25(1) (*b*), introduced in April, 1962, SFCs may guarantee deferred payments due from any industrial concern for indigenous purchase of capital goods. IFC too has been authorised to extend such guarantees, in terms of Sec. 23(1)(*b*)(*ii*) of the IFC Act. No such guarantees have been issued so far by either SFCs or IFC. As stated earlier, these guarantees must also be "sufficiently secured". The guarantee of foreign deferred payments has been left over to IFC. Perhaps no guarantees for indigenous purchases have been issued so far due to the unwillingness of the machinery manufacturers or dealers to offer deferred payment terms beyond a very short period in view of the demand conditions, as in a sellers' market for capital goods, prevailing in India at present. There does not, therefore, appear to be much scope for SFCs to develop this business in the circumstances obtaining at present; though if they could extend the sphere of their activities to this field, they could increase their income without direct financial commitment.

(*iii*) Direct subscription to debentures

V.68. Sec. 25 (1)(*g*) of the Act permits SFCs to subscribe to the debentures of an industrial concern, repayable within 20 years from the date on which they are subscribed to. If such debentures carry an option for subsequent conversion into stock or shares of the concern, SFCs may exercise such option and acquire such stock or shares in accordance with, and subject to, the provisions of Section 81 of the Companies Act, 1956. As on 29th March, 1963, Andhra Pradesh, Mysore and Gujarat SFCs had subscribed to debentures of the order of Rs. 8.55 lakhs, Rs. 10.00 lakhs and Rs. 3.75 lakhs respectively. The operations of SFCs in this respect

have been discussed in detail under "Investments" where we have made certain recommendations for increasing this business.

(iv) Underwriting

V.69. Underwriting has arisen as a means of protecting borrowing concerns from the vagaries of the investment market—of ensuring the possession of adequate funds at the time they are needed, and at a reasonable cost. The practice in underdeveloped countries like India differs widely from that followed in advanced countries. Underwriters in Wall Street, for instance, perform essentially a marketing function. They intend and expect to dispose of all the securities they underwrite, and consider the operation unsuccessful if a large amount is left on their hands. Elsewhere, underwriting, at least as practised by development banks, combines investment and marketing functions. Thus, ICICI tries to attract as much private interest in the issues as possible but does not agree to underwrite unless it is prepared and willing to keep in its portfolio, if necessary, the full amount of the issue underwritten by it. To the extent private capital is attracted, it feels it has performed a useful function, even though it retains a large part of the issue. It sells shares out of its portfolio only gradually, and in small quantities, to avoid depressing their price, in the interests of the enterprise and other investors in it. The demonstrable success of the enterprise and reasonable prospects for its future are necessary preconditions before ICICI disposes shares retained in its portfolio. The disposal of such shares has so far yielded handsome profits.

V.70. In terms of Sec. 25(1)*(c)* of the Act, SFCs may underwrite the issues of stock, shares, bonds or debentures by industrial concerns. Under Sec. 25(1)*(f)*, a SFC may retain, as part of its assets any stock, shares, bonds or debentures which it may have to take in fulfilment of its underwriting liabilities, so however, that it disposes of them as early as practicable, but in no case beyond 7 years from the date of their acquisition, except with the prior permission of Reserve Bank. As stated earlier, only since the amendment of 1962, SFCs are permitted to retain the securities beyond 7 years. This relaxation may now induce them to enter this business.

V.71. This question of underwriting was considered at the Third, Fourth, Seventh, Eighth and Ninth SFCs' Conferences. The Third Conference, in 1956, set up a Committee of representatives of IFC and some SFCs to formulate certain suggestions. The Committee was generally in favour of SFCs venturing into the field. It recommended that initially they should underwrite fixed interest-bearing industrial securities i.e. debentures and preference shares of redeemable type with rights for cumulative dividend, to minimise the risks of loss of income and probable depreciation in capital value. The Fourth Conference which considered the Report of the Committee felt that in view of the risks involved it was not yet desirable for them to enter the field. The Seventh

Conference considered a suggestion to set up a consortium of financial institutions to sponsor large public issues by industrial concerns, but it was not accepted. The question of underwriting came up again at the Eighth Conference in 1961 in the context of the programme of industrialisation envisaged under the Third Plan, during which period many new industries were scheduled to be developed in the private sector. While generally reiterating earlier decisions, this Conference agreed that some SFCs might make a small beginning in underwriting issues provided they exercised caution and observed certain safeguards. The general considerations and precautions to be taken by SFCs as contained in the Reserve Bank's note (prepared on the suggestion of the Eighth Conference) were accepted by the Ninth Conference for serving as guide lines to SFCs. So far, West Bengal SFC and ICICI have jointly underwritten in 1962 shares of an engineering unit to the extent of Rs. 5 lakhs and Rs. 7 lakhs respectively. Further, Rajasthan SFC has underwritten the shares of an industrial concern (textile mill) in 1961-62 to the extent of Rs. 5 lakhs, out of a total amount of Rs. 30 lakhs underwritten by various parties, including IFC and LIC. No other SFC has yet entered this field. Rajasthan SFC is not now in favour of undertaking this type of activity because it had to take up shares of the value of Rs. 4.91 lakhs in fulfilment of the underwriting obligation. No doubt, it has taken personal guarantee of two respectable persons (presumably promoters), who have undertaken to re-purchase the shares which may remain unsold and to pay deficit in dividend, if any, at 7½% per annum at the end of 5 years. But its funds have been locked up in the meanwhile and it will not get interest unless dividend is declared by the mill. Our recommendations in regard to the operations of SFCs in this field have been furnished under "Investments".

Appendix to Chapter V

Industry-wise Breakdown of Loans and Advances

The major groups of industries to which the Corporations had made loans and advances have been indicated in the body of Chapter V. Certain details (as on 31st March, 1963) regarding these advances in the different States are given in this Appendix.

(A) Advances to Small Scale Units—Rs. 703 lakhs for all Corporations

"Traditional" industries :—food manufacturing etc. and cold storage

Advances to cold storages—under food manufacturing industries—are found mainly in the three States of Bihar, Punjab and Uttar Pradesh. On 31st March, 1963, Bihar SFC had effective sanctions of Rs. 32 lakhs on as many as 31 applications. Most of this amount had been sanctioned to partnership and private limited concerns. Proprietary (5) and joint Hindu family (2) concerns got about a fifth of the total. Even on this date, the SFC had overdues of Rs. 2.5 lakhs in its books. How far this is due to either uneconomical size of the plants, or excess capacity, or faulty management, needs looking into.

In Punjab and Uttar Pradesh too, the bulk of advances is to partnership concerns, and the average size of advances sanctioned is quite small. Small overdues have arisen in Uttar Pradesh.

Miscellaneous food preparations

Miscellaneous food preparations cover a wide range of industries: canning and preservation of fruits and vegetables and fish, etc.; flour, rice and dal mills; sugar factories; manufacture of edible oils and of hydrogenated oils, etc. (the last, and also manufacture of sugar, involving much capital investment, are not usually to be found in the small unit sector). Loans to small units are still largely for edible oil, rice and dal mills in Andhra Pradesh. In Orissa, they are mainly for rice mills while in Kerala, some loans are for cashewnut processing too; but both in this as also in the loans for edible oil making, overdues have arisen.

Tea

Outstandings for tea manufacture are almost wholly in Assam. Almost 75% of the amount in Assam is due from proprietary gardens, the average value of sanctions being about Rs. 2 lakhs. Advances to private limited gardens are even smaller. Small overdues are seen here.

Textiles

Textiles manufacture accounts for 4.6 per cent of the total outstandings from small units. Punjab alone accounts for about one fourth of this group—and bulk of this is under non-cotton textiles—mainly wool. Other Corporations which figure prominently are Maharashtra, Mysore and Madhya Pradesh. While more than one-half of loans outstanding in the first two Corporations is from units in textile other than cotton, those of the last are mainly from cotton textiles units. Loans of Madhya Pradesh Corporation are mainly concentrated in ginning, cleaning and pressing, and nearly one-half of Mysore loans is outstanding in respect of art silk (average value of sanction being as small as Rs. 26,500). Kerala also has shown certain loans for coir manufacture.

"Non-traditional" industries :—chemicals

Maharashtra occupies an important position in the chemicals group (35% of the total), other important States being Andhra and Madras. In Maharashtra, in recent years there seems to be a shift towards drugs and pharmaceuticals, and fertilizers; small overdues have arisen in this group as on 31st March, 1963.

Non-metallic mineral products, except petrol and coal

This group was seen to account for about eight per cent of the total outstandings. The Madras Corporation has no outstandings in this group. Mysore leads here, with over 80% of the total being for tiles, most of which are very recent advances. Firebricks also claim a small amount. Tiles are the most important category in Kerala as well. In Bihar most of Rs. 5.04 lakhs is under the sub-groups sanitary and whiteware, insulators and firebricks—all relatively recent advances. Punjab has one substantial account in prestressed roofing and insulating slabs. Other Corporations having relatively significant outstandings in this group are Gujarat, Maharashtra and Orissa. While Gujarat's outstandings are mostly from units manufacturing sanitary and whiteware, chinaware and pottery, those of Maharashtra are mostly from units engaged in manufacture of glass and glass products, bricks and tiles. Advances of Orissa are to units manufacturing hume pipe, cement and concrete products besides sanitaryware and whiteware.

Basic metal industries :—Iron and Steel, and non-ferrous

As would perhaps be expected, the outstandings in this group are well distributed among different States, three of which claim a tenth or more of the total—Madhya Pradesh, Mysore and Punjab, with Mysore leading. Almost all the outstandings constituting 10.6% of total are in iron and steel basic industries. The average size of sanctions in this group for the above three States is about Rs. 1 lakh.

Metal products, except machinery and transport equipment

Over eighty per cent of loans outstanding in this group is in the six States of Maharashtra, Assam, Madhya Pradesh, Punjab, Rajasthan and Andhra, in descending order of the amounts. This group includes a large variety of activities: bolts, nuts, screws and nails; metalware and utensils, hand tools and small tools; metal containers and trunks; weights; cutlery, locks, etc., type pounding; sanitary and plumbering fixtures and fittings of metal, expanded metal.

Machinery, except electrical machinery

This again is a very wide group, including machinery for paper, dal, flour and rice mills; internal combustion engines; agricultural implements; textile machinery; vacuum cleaners; tractors, harvesters, etc.; sewing and knitting machine tools. Maharashtra leads in this group and Punjab is a close second. With Uttar Pradesh also included, these three States account for seventy per cent of the total in the group. The average size of sanctions in Punjab is over Rs. 2 lakhs, while it is about half-a-lakh in Maharashtra. Most of the borrowing units of the latter would be making, therefore, components for these different kinds of machines.

Electrical machinery and transport equipment

Maharashtra leads in the group "electrical machinery, apparatus, appliances, and supplies" as well, mainly in household appliances, radio receivers including amplifying and public address equipment, equipment for general transmission, etc. Other Corporations having more than one-tenth of loans in this group are Punjab and Rajasthan. In "transport equipment", however, Punjab comes first, with advances for manufacture (or assembly) of motor cycles and bicycles, and other transport equipment and components.

The above gives a broad idea of the industry-wise breakdown of total outstanding loans to small scale units, indicating the States where particular types of industries have received finance. Before taking a similar look at the outstandings from "other", i.e. medium and large-sized units, we may look at the small units' loans from another point of view, viz., the industry-wise breakdown of these loans in some of the major States, considering one at a time.

Industry-wise breakdown of advances in certain States

In terms of the magnitude of the outstanding loans to small units, the more important States are Maharashtra, Punjab, Assam, Mysore, Andhra, Bihar and Madhya Pradesh.

Over 50% of the loans in Maharashtra is for chemicals (including drugs, etc.), metal products, and electrical and other machinery. In Punjab too, there is a fairly wide spread, the more important groups being cold storage, woollen textiles, iron and steel basic industries, manu-

facture of miscellaneous machinery—both electrical and others, and transport—mainly cycles, etc. Assam has, besides tea, metal products (not machinery), a sizable amount in wood and cork—mainly from concerns engaged in saw milling, including timber treating, and plywood manufacture for tea chests. In Mysore, tiles have absorbed about one-fourth of the total, followed by iron and steel basic industries, rice mills, art silk and edible oils. In Andhra, miscellaneous food preparations account for about a quarter of the total—mainly rice mills and manufacture of edible oils (other than hydrogenated). Next in order of importance are chemicals (including fertilizers), metal products (excluding machinery) and (not listed in table)—lithographic printing and litho press and printing of dailies, straw board, etc. About one-half of the amount in Bihar is for cold storage, rest being in insulators, sanitary and whiteware, firebricks and refractories, iron and steel basic metal industries, etc. In Madhya Pradesh, more important groups are iron and steel basic industries, manufacture of metal products, cold storage and cotton textiles.

(B) Advances to Other Units (Not Small Scale)—Rs. 2703 lakhs for all Corporations

"Traditional" industries : food manufacturing, etc., sugar, tea, and cold storage

Bihar, Madras, Uttar Pradesh, West Bengal, Andhra and Rajasthan among them account for the bulk of the outstandings under sugar. In Bihar, these are all to public limited companies, the average value of sanctions being Rs. 7.7 lakhs. These are recent loans, only about 10 per cent having been repaid by 31st March, 1963. In Madras, the entire sum of Rs. 19 lakhs to this industry is due from two companies only. In Andhra, the entire sum is due from a co-operative sugar factory.

In tea manufacture, Assam accounts for about 60 per cent of the total for all Corporations, and Kerala for another 27 per cent. West Bengal's outstandings constitute about 8% of the total. Madras and Uttar Pradesh—other tea producing States—are significant omissions.

In cold storage, West Bengal comes first, followed by Bihar, Uttar Pradesh and Punjab. Average sanction is about Rs. 3 lakhs in West Bengal, though partnership and proprietary concerns have also got the loans, and almost Rs. 4 lakhs in the case of Uttar Pradesh. The loans in Bihar are only of medium-size, the average sanction being for Rs. 1.6 lakhs.

Miscellaneous food preparations

The miscellaneous food sub-group is the largest in this group, and Madras holds an important position followed by Andhra, Mysore, Assam and Rajasthan. Madras alone accounts for about two-fifths of the total, composed of large sums for flour mills, hydrogenated oil, glucose, etc. largely in public companies. Andhra, Mysore and Assam come next in

order. Andhra has large sums for flour mills and hydrogenated oils. In Mysore, they are largely for hydrogenated oil and coffee curing works. In Assam, the entire sum is for flour mills, given in the last few years.

Textiles

The textiles group is dominated by Madras, which accounts for nearly 60 per cent of the group total, and 67 per cent of the total for cotton textiles. Also, of the total outstanding loans of the Madras Corporation (small as well as other units) on 31st March, 1963, textiles alone form fully 46 per cent. The bulk of the textiles loans is to a large number of public spinning and weaving companies, private companies and partnerships accounting for less than a third. Rajasthan, West Bengal, Mysore, Kerala, Orissa and Madhya Pradesh too have sizable outstandings in cotton textiles (but only a fraction of the amount in Madras). The relatively smaller amount of Rs. 98 lakhs for textiles other than cotton is made up largely of outstandings in Andhra, Punjab and Maharashtra. Andhra has shown the advances to three co-operative and one public limited spinning mills. Art silk figures prominently in Maharashtra.

"Non-traditional" industries :—Machinery, except electrical

This group is the most important among the "non-traditional" industries. About 9 per cent of the outstandings of the 15 Corporations is in this machinery group, of which Madras alone has contributed 45 per cent, followed by Punjab, Maharashtra, West Bengal and Kerala. Madras has reported 9 sanctions to 5 public companies and a trust for an average size of about Rs. 15 lakhs for textile, sugar and paper machinery, engine valves and machine tools, etc. with total advances of Rs. 110.4 lakhs. Textile machinery (carding machines), machine tools and internal combustion engines are the major sub-groups in Punjab, reflecting the regional development of woollen textiles and of small scale mechanical enterprises. In Maharashtra, understandably perhaps, over one-half of the Rs. 36 lakhs due is for textile machinery, followed by agricultural implements and machine tools. In West Bengal, two accounts—one to a private company for machine tools, and other to a public company for typewriters and duplicators—make up four-fifths of the total. In Kerala, the amount is almost equally divided between one private and one public company, engaged in making agricultural implements and machinery respectively.

Chemicals, etc.

As in the case of small units, Maharashtra has recorded here the largest outstanding, 45 per cent of the total for 14 SFCs, and 38.8 per cent for all the 15 Corporations. Next in importance are Madras, West Bengal, Andhra and Gujarat. In Maharashtra, numerous concerns in the following sub-groups in particular have been financed—drugs and

pharmaceuticals, vegetable oils including solvent extracted oils; paints, varnishes; polythene vide films, and ink. As in most other categories, the amount in Madras is outstanding from only a few firms, one public company alone owing the bulk of the amount for manufacture of calcium carbide (sanctioned amount Rs. 22.5 lakhs). In West Bengal, vegetable oils (including one sanction of Rs. 9.5 lakhs to a proprietary concern), drugs, synthetic resins and plastics, paints and varnishes and ink, etc. form the major groups, the average size of sanctions being about Rs. 5 lakhs. In Andhra, solvent extraction in particular has accounted for one-half of the sanctioned amount, followed by drugs and fertilizers. Almost the entire outstanding in Gujarat is for vegetable oil, including solvent extracted oil, given largely to proprietary and partnership concerns.

Non-metallic mineral products

In this group, out of the total outstandings of Rs. 1.44 crores, Madras, Bihar, West Bengal, Kerala, Maharashtra and Punjab account for 22, 12, 12, 11, 10 and 10 per cent respectively. Rs. 15 lakhs, out of Rs. 31.10 lakhs due in Madras, are from one partnership concern in refractories —rest are largely in bricks and tiles and mica. In Bihar, the total is made up of loans mainly for fire bricks—of which about two-thirds are to public limited companies. Almost 50 per cent of the total in West Bengal is due from one public company in refractories. In Kerala, tiles account for the bulk of the outstandings, rest being for bricks and pottery. In Maharashtra, about Rs. 10 lakhs and Rs. 4.7 lakhs are outstanding from public limited and partnership concerns engaged in manufacture of grinding wheels and abrasives, and glass and glass products respectively. In Punjab, fire bricks, refractories, frigwool and glasswool are prominent.

Basic metal industries

The "basic metal industries" group ranks below the "machinery except electrical" and "chemicals" groups in the "Other" industrial units sector, unlike the outstandings with small units. But, like the latter, here too the non-ferrous sub-group is insignificant and features almost wholly in Bihar and Punjab. This is largely due to (*a*) the general shortage of non-ferrous metals, the indigenous production of which is negligible as compared with the requirements which have expanded at a fast rate in the context of the successive Five Year Plans, and (*b*) the relative inexperience of many producers with processes of handling these metals. In the ferrous group, Punjab, Bihar and Assam have contributed sizable sums. For the ferrous group, Punjab records only a small number of accounts, the average size of all sanctions being no less than Rs. 8.9 lakhs, including sanction of Rs. 20 lakhs to 2 public limited companies. In Bihar, all loans are for casting and forgings to four public companies. Structurals (4 accounts) and pipes (2 accounts for

Rs. 10 lakhs) make up the total in Assam. Casting and forgings may not be economical in this State because of the cost involved in carriage of the bulky raw materials from other parts of India.

Transport equipment

As in the case of advances to small units, here too Punjab occupies the first position in the transport group. Madras comes second, followed by Bihar and Assam. Manufacture of motor cycles and bicycles, railway rolling stock and miscellaneous transport equipment make up the total of Rs. 33.50 lakhs in Punjab. In Madras and Assam, amounts of Rs. 27.45 lakhs and Rs. 18.50 lakhs respectively are due from a public company in wagon making and 3 public limited concerns in cycle (and parts) making respectively. Four public companies in motor cycle and cycle (1) and railway rolling stock (3) owed Bihar SFC Rs. 19.9 lakhs. An overdue of Rs. 1.1 lakhs was reported in Bihar on 31st March, 1963.

Paper and paper products

In paper and paper products, Bihar, Gujarat, Madhya Pradesh, Maharashtra, Punjab, Uttar Pradesh, West Bengal and Madras account for almost all the outstandings. As paper manufacture usually requires considerable capital investment, most borrowing concerns are public limited companies, except some partnerships in places like West Bengal.

Metal products, except machinery and transport equipment, and electrical machinery

About one-third and one-fourth of the Rs. 78.4 lakhs outstanding in 'metal products' group with all the Corporations are accounted for by Maharashtra and West Bengal respectively. In the electrical machinery group—Rs. 113.2 lakhs for all Corporations—Madras and West Bengal account for 40% and 29% respectively. If former is excluded, West Bengal would account for about 50% of the total for SFCs.

Industry-wise breakdown of advances in certain States

As was done in the case of advances to small scale units, those to the medium and larger units may also be considered from the point of view of their industry-wise breakdown in some of the major States, considering one at a time. In terms of the magnitude of the outstanding loans to these other units, the more important States are—apart from Madras which also accounts for almost exactly one-half of what all the 14 SFCs have achieved—Maharashtra, West Bengal, Punjab, Assam, Bihar and Kerala, with outstandings of over Rs. 1.25 crores each.

In Maharashtra, about 30 per cent of the advances are in the chemicals group, followed by manufacture of machinery except electrical machinery, metal products, textiles other than cotton and manufacture of electrical machinery. There is perhaps a more even distribution in West Bengal, despite almost one-fourth being for cold storage and

cotton textiles; reflecting the development of metal industries in this State, one finds a fair spread of about a third of the total in these three groups—metal products except machinery and transport equipment, machinery except electrical machinery, and electrical machinery, apparatus and appliances. Over one-half of the advances in Punjab is in basic metal industries (mainly ferrous), machinery except electrical, and transport equipment. Assam is heavily committed to tea, followed by—a long way behind it—electricity supply, transport equipment, iron and steel basic industries, wood and cork and non-metallic mineral products. In Bihar, about 39 per cent of the total are in food industries—mainly sugar and cold storage; basic metal industries, transport equipment, paper and non-metallic mineral products are other industries which have received assistance. About one-third of the advances in Kerala is in food manufacturing and about one-fourth in cotton textiles; manufacture of non-metallic mineral products, rubber products and machinery have also been financed.

CHAPTER VI

WORKING RESULTS, FISCAL CONCESSIONS, MANAGEMENT, ETC.

Working results and fiscal concessions

VI.1. We have now undertaken, as required by the terms of reference, a broad review of the major facets of SFCs, except their working results. This will now be taken up. Following from this, we examine the two recent fiscal concessions that the Central and State Governments and the Reserve Bank of India have extended to SFCs as being considered necessary to ensure their efficient functioning. These concessions do not measure up to what we consider as the minimum to which these institutions are entitled, in view of their statutory obligations and of their peculiar teething troubles for which even in foreign countries such institutions have been given various special facilities, as we have already seen. We give, therefore, in conclusion, our own recommendations in this matter, for some of which we may have already provided certain indications.

VI.2. As compared with the position in 1961-62, many SFCs have shown considerable improvement in their working during 1962-63. At the end of March, 1962, SFCs had about Rs. 28 crores of resources, comprised of paid-up capital, bonds and other borrowings (excluding sums advanced by State Governments for loans to small scale units). On that date the outstanding loans and advances were no more than Rs. 18.65 crores. This gap between resources and their employment in loans was markedly narrowed down by March, 1963, when, with resources of about Rs. 31 crores, the outstanding loans had gone up to Rs. 25 crores. This is reflected in considerably larger income as interest on loans. The grand total of the Profit and Loss Account for all SFCs had jumped by over Rs. 50 lakhs to Rs. 178 lakhs during 1962-63, over 90% of which is due to higher interest income from loans. The breakdown of the consolidated Profit and Loss Account among the major items is shown below for the two years. Interest on loans—Rs. 1.41 crores—now forms 80% of the total income, and interest on investments—17%. Latter shows large variation among different SFCs in relation to the former—reflecting both the mode of investment of surplus funds, and the dexterity with which paid-up capital and resources raised by bond issues have been used in giving loans which yield higher returns than investing in trustee securities or depositing with banks. Thus, while in 1961-62 interest on investments amounted to 28% of that on loans for all SFCs, this proportion varied all the way from 10% in Assam, 12% in West Bengal, 13% in Punjab and Kerala, and 17% in Bihar to 34% in Maharashtra, 56% in

Consolidated Profit and Loss Account of SFCs.

(Rs. lakhs)

Income	1961-62	%	1962-63	%	Expenditure	1961-62	%	1962-63	%
Interest on loans	95.63	75	141.18	80	Interest on bonds	39.31	31	73.14	41
Interest on investments	27.07	21	31.29	17	Staff salaries, etc.	19.47	15	22.41	13
Miscellaneous income	4.66	4	5.52	3	Miscellaneous	2.86	2	2.71	2
					Balance of Profit and Loss account	65.72	52	79.73	44
Total	127.36	100	177.99	100	Total	127.36	100	177.99	100

Andhra, 72% in Mysore and 78% in Gujarat. In almost all the latter States, the proportion has fallen in 1962-63. The former set of States has maintained their ratios, except Kerala where it is 28%. Since all SFCs except those of Jammu & Kashmir and Orissa have to depend now on bonds for further lending, they are expected to employ their resources to the maximum extent for loans and to regulate the raising of resources accordingly. In this, they will be helped also by the provision for borrowing from Reserve Bank pending bond issues.

VI.3. The increases of Rs. 34 lakhs in interest on bonds and of about Rs. 3 lakhs in staff salaries, directors' fees, etc. are the two most important developments among items of expenditure. Former has taken away the bulk of the gain in interest income. On 31st March, 1963, twelve SFCs had bonds of Rs. 16.15 crores outstanding, against Rs. 12.18 crores a year earlier. Nevertheless, the balance of profit taken to the appropriation account shows an increase of Rs. 14 lakhs over 1961-62.

VI.4. Salaries and allowances of staff and directors, and other establishment charges have gone up from an average of Rs. 1.4 lakhs in 1961-62 to Rs. 1.6 lakhs in 1962-63, or by 14%, well over one-half of which would perhaps be due to increments in salaries to existing staff. The range of these expenditures in the former year was from Rs. 0.55 lakh in Orissa to Rs. 2.88 lakhs in Maharashtra; in 1962-63, Rs. 0.64 lakh in Orissa to Rs. 3.76 lakhs in Maharashtra. But even at Rs. 1.6 lakhs, the average of establishment charges is still on the low side, as most SFCs have tried strictly to keep down their establishment expenses to reduce subventions.

VI.5. The consolidated appropriation account for all SFCs is shown below. Even if no sums were put away for reserves, taxes and guaranteed dividends would together have fallen short of profits in the two years by Rs. 11 lakhs and Rs. 6.47 lakhs respectively. Since Rs. 5.35 lakhs and Rs. 9.16 lakhs were credited to reserves, SFCs drew subventions of Rs. 16.35 lakhs and Rs. 15.63 lakhs in the two years, raising the total

Consolidated Appropriation Account of SFCs.

(Rs. lakhs)

	1961-62	1962-63
To Taxation	30.34	37.55
To Statutory Reserve Fund	0.83	0.92
To Special Reserve Account	3.93	7.23
Other Reserves	0.59	1.01
Total	35.69	46.71
Balance of Profit	65.72	79.73
Available for Dividends	30.03	33.02
Subvention from State Governments	16.35	15.63

subventions to date to Rs. 1.62 crores. Only Assam SFC could have done without the subvention of Rs. 0.7 lakh in 1962-63 if it did not transfer Rs. 0.75 lakh to the Special Reserve Account to take advantage of the remission of tax on such transfers.

VI.6. The position since the SFCs commenced business seems to be, in broad magnitudes, that upto 1962-63 they made a total profit of Rs. 4.38 crores of which provision for taxation took away Rs. 1.96 crores. Post-tax profits of Rs. 2.42 crores, supplemented by subventions from the States of Rs. 1.62 crores, were appropriated as follows—to dividends Rs. 3.72 crores, and to reserves Rs. 0.32 crore. Out of the dividends of approximately Rs. 2.36 crores (63.8% of Rs. 3.72 crores) received by the States and Reserve Bank, they have so far forgone/agreed to forgo Rs. 0.15 crore towards the Special Reserve Fund.

VI.7. It may be noted that the volume of business of these institutions was not sufficient to pay dividend even at the low rate of 3/3½/4%. It is only recently that *three* of them have been able to pay dividends without Government subventions. The State Government's guarantee for minimum dividend to institutional investors was an understandable provision as otherwise they would not have contributed to the share capital. But this consideration did not apply to the States and Reserve Bank. It is an odd situation that they have been drawing dividends when profits did not justify it. Looked at from another angle, the purpose of this requirement of payment of minimum dividend might have been to ensure that SFCs adopted normal business policies and met business tests of success. As, however, these institutions partake of the nature of development banks, which requires them to take risks which normal lending institutions are unwilling to assume, charge relatively low rates of interest, and are able to transact only a limited volume of business in the less industrialised States, it was only fair not to enforce

this dividend requirement with respect to the capital held by the States and Reserve Bank. As this was not done, SFCs have built up a huge subvention liability to finance the payment of dividends. This means that they never had the advantage of equity share capital on which they could skip dividend ; and they were liable to pay corporate tax on profits which would not be there had the loan character of the share capital (inherent in a guaranteed dividend) been recognised.

VI.8. The result has been that even almost after a decade, SFCs have not built up adequate reserves; and consequently they have, by and large, avoided taking calculated risks and financing new enterprises in untried fields—purposes for which they were set up. Unless their business increases very substantially in the next few years, there does not seem much prospect of reserves increasing rapidly as the first charge on profits after taxes and dividends would be the repayment of the subvention liability to State Governments.

Fiscal concessions—The two concessions which SFCs have received in recent years, viz., the tax exemption on 10% of their profits to be credited to a Special Reserve Account, and the creation of a Special Reserve Fund (under Sec. 35A of the SFCs Act as amended in 1962) to which would be credited such part of their dividends which the State Governments and Reserve Bank might agree to forgo, have been already indicated in Chapter III. Some such concessions were needed much earlier. It was also argued in Chapter III that to enable SFCs to build up necessary reserves at not too slow a pace, these two concessions should be further extended—by increasing the maximum tax-free appropriations to the Special Reserve Account in any year to a higher figure than 10% now permitted (subject to the ceiling of total permissible transfers), and by increasing beyond 10% of the paid-up capital the ceiling of accumulations in the Special Reserve Fund. But neither of these can really solve their basic difficulties to which we now turn.

VI.9. In 1948, i.e. three years before the SFCs Act was passed, Government had set up the IFC for supplying term credit to public limited companies and industrial co-operatives. The main object of having complementary SFCs was, broadly, to perform a development function—to promote the growth of the sectors of small and medium-sized industrial units in the different States, organised as proprietary and partnership concerns, in addition to limited companies, by providing them equipment loans at reasonable cost, as also to generally guide these units in the early stages in appraising their prospects, etc. To build up a sizable volume of advances so that a lending institution like a SFC becomes—within a reasonable time—a viable economic unit i.e. one that is able to pay its way, give its bond and shareholders a reasonable return, and can gradually accumulate reserves to buttress its financial position and absorb shocks due to defaults, is a time-consuming process. For SFCs, the difficulty was further aggravated by a few other factors like the ceiling on total assistance to an industrial concern already

mentioned above; the exhortation to lend increasing amounts to small scale units at low rate of interest, without considering if such loans were profitable from the institutions' point of view; providing for guaranteed dividend on the shares of these institutions—including the large blocks held by the State Governments and Reserve Bank—at a predetermined rate right from the commencement of business; and making no allowance for a gestation period and subjecting their profits to tax on normal basis.

VI.10. The net results of the heavy burden of taxes and guaranteed dividends have been that, as we saw above, only very meagre reserves have been built up so far; there is a dead-weight burden of subvention liability to State Governments of no less than Rs. 1.62 crores as on 31st March, 1963, which is still growing—the addition in 1962-63 being Rs. 16 lakhs (Table XIII). With such meagre reserves and the subvention liability which has effectively mortgaged their future profits, SFCs find themselves unable to enter new lines of business or take calculated risks for fear of any loss which such new ventures may involve.

VI.11. As development banks operating in the milieu of a relatively under-developed economy, SFCs should have been extended suitable tax concessions even when they were set up. The present very serious weaknesses would then never have developed. SFCs are entitled to a further measure of consideration for their efforts in helping the small scale sector of Indian industry—efforts which are really of the nature of furthering a national policy. As on 31st March, 1962, this sector absorbed fully 31% of the total advances sanctioned. After over a decade's experience in promoting small scale units in Indian industry, it is now evident that, while the provision of transport, power, etc. is no doubt vital, a major determinant of growth is the adequacy of finance—both in the form of equity and equipment loans. Lending institutions which serve this sector have to be accorded special treatment, often of a far-reaching nature, if sizable results are being aimed at. Owing mainly to the small size of loans in this sector, and the often tortuous legal scrutiny of assets offered for them as security, to make, as also service, these loans are uneconomic if such services are to be provided at low rates of interest irrespective of the cost to the institutions. SFCs have received none of the concessions like the development rebate or tax holiday given to industrial concerns (7 years for co-operative sugar factories and 5 years for joint stock factories) though it is not difficult to make out plausible cases for such concessions because of the special nature of the business entrusted to these institutions and the practices followed in many foreign countries (Appendix I). Except in one case, we have not found any foreign development bank having a liability for guaranteed dividends. On the other hand, many have received tax concessions and, in other cases, their earning potential has often been enhanced by the State providing substantial interest-free, or low interest bearing, funds to be used for loans and advances; SFCs have lost on all these counts.

TABLE XIII

Subventions availed of by State Financial Corporations.

(Rs. lakhs)

Sl. No.	Corporation of	Date of establishment	Paid-up capital	Rate of guaranteed dividend %	Net profit subject to provision for taxation, reserves, etc. in 1962-63	Subvention from the State Government for guaranteed dividend	
						Required for 1962-63	Total amount received so far (including requirements for 1962-63)
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
1.	Punjab	1- 2-1953	100	3	8.26	—	10.25(a)
2.	Kerala	23-11-1953	100	3½	5.06	1.41	11.38
3.	Maharashtra (Reconstituted)	30-11-1953	100	3½	8.12	—	28.68(b)
4.	West Bengal	1- 3-1954	100	3½	7.49	—	11.87
5.	Assam	19- 4-1954	100	3½	7.47	0.66	10.30
6.	Uttar Pradesh	25- 8-1954	100	3½	4.78	1.42	12.37
7.	Bihar	2-11-1954	100	3½	6.25	0.82	11.12
8.	Rajasthan	17- 1-1955	100	3½	5.19	1.10	12.17
9.	Madhya Pradesh	30- 6-1955	100	3½	4.19	2.02	12.80
10.	Andhra Pradesh (Reconstituted)	3-11-1955	150	3½	8.07	1.75	19.99
11.	Orissa	20- 3-1956	100	3½ & 4	4.15	0.77	4.72
12.	Mysore	30- 3-1959	100	4	4.85	2.14	8.37
13.	Jammu & Kashmir	2-12-1959	50	4	1.07	1.59	4.56
14.	Gujarat	1- 5-1960	100	3½	4.78	1.95	3.86(c)
			1400		79.73	15.63	162.44

(a) The Corporation has repaid Rs. 26,025 to the State Government in partial liquidation of subvention liability.
(b) Inclusive of the amount of subvention transferred to Gujarat SFC during the year.
(c) Exclusive of the amount of subvention transferred by Maharashtra SFC during the year.

There have been recently belated, as also meagre, attempts to make up for this.

VI.12. In view of the many handicaps under which SFCs are operating, as also of such factors as a measure of slackening of industrial activity due to shortages of foreign exchange, power, transport, cement, etc., some of which may persist, no very spectacular growth in the business of SFCs can be expected. But the financial position in which many SFCs find themselves today and which they are likely to experience for some more years is not one that can be allowed to continue with equanimity. The issue, thus, is not merely to look for tax concessions. Other supplementary financial concessions are needed so that these institutions become fit instruments to attain the objectives for which the legislators set them up.

VI.13. In the realm of tax concessions, the only one so far extended by the Central Government came fully 10 years after the SFCs Act of 1951. Perhaps taking the cue from what the Government of Pakistan had legislated in 1960 for their recently set up Pakistan Industrial Credit and Investment Corporation, our own Finance Act of 1961 provided that certain term lending institutions to be specified by Government could annually credit upto 10% of their profits to a Special Reserve Account till such time as the amounts so credited to this Account add up to the paid-up capital; amounts so credited would be tax-free. This is a welcome concession, but a very meagre one. Many SFCs are still making small profits. Certain tentative calculations show that even on the very favourable assumption that these institutions continue to *increase their net profits in the future at the same rates that they have done in 1960-61 to 1962-63* when business expanded for most of them at a considerably faster rate than before (total profits of all SFCs during 1960-63 were over 36% above the level during 1957-60), it would take a few decades for credits to the Special Reserve Account to add up to the paid-up capital. As the footnote to the table below (Table XIV) will show, this assessment of the concession is based only on the more favourably placed institutions.

VI.14. This concession consists of (*a*) an exemption from tax of 10% of profits and (*b*) giving this exemption for credits upto the paid-up capital. Now if part (*b*) is retained, but (*a*) is relaxed, i.e. higher annual tax-free deductions within the ceiling as in (*b*), the Government of India, which have agreed to this concession upto the paid-up capital, would presumably not only not lose, but may even gain in the long run. If, say, the entire profits are exempted, that would, in effect, be only telescoping into a shorter period a benefit they have agreed to confer, but spread over a considerably longer time-span. In the long run, this further concession will yield more revenue to Government by enabling SFCs to earn more by expanding their business faster, and by having a higher taxable profit on loans made out of funds in this Account than out of interest bearing borrowed funds.

TABLE XIV

Assessment of the tax concession provided in the Finance Act, 1961.

Corporation of	Paid-up capital (Rs. lakhs)	Average profits (before tax) for the period 1960-61 to 1962-63 (Rs. lakhs)	Annual average rate of growth of profits during 1960-61 to 1962-63 (%)	Number of years for the Special Reserve Account to equal paid-up capital
(1)	(2)	(3)	(4)	(5)
Assam	100	6.70	11.32	27
Bihar	100	5.51	16.61	22
Jammu & Kashmir	50	0.76	43.74	18
Madhya Pradesh	100	4.07	3.41	67
Mysore	100	4.10	17.52	23
Orissa	100	2.74	52.70	12
Punjab	100	6.72	24.77	16
Rajasthan	100	4.67	10.31	32
West Bengal	100	6.80	11.99	26

(NOTE: This exercise had to be limited to these nine SFCs which showed increases of net pre-tax profits in both 1961-62 and 1962-63. Of the remaining SFCs and MIIC, Gujarat came in existence only in May, 1960 and the other SFCs and MIIC showed decreases in profits in either 1961-62 or 1962-63 as compared with the immediately preceding year.)

VI.15. But as long as the post-tax profit of any SFC is below its dividend liability, and it has to continue to draw subvention from the State to meet such liability, any credits to this Account out of profits would mean drawing pro tanto more subventions, except for the saving in income tax on such credits.

VI.16. But there is another side to this. The State Governments and Reserve Bank now hold about 63.8 per cent of the shares of SFCs. Tentative calculations have indicated that since inception SFCs have paid to these holders about Rs. 2.36 crores as dividends. Thus, not only the entire subvention of Rs. 1.62 crores but an additional sum of Rs. 0.74 crore out of the post-tax profits of SFCs has been paid out to the States and Reserve Bank. It was to remedy this anomalous situation that in December, 1959, Reserve Bank recommended to the States the creation of a Special Reserve Fund for which it volunteered to forgo the entire dividends accruing to it if the States agreed to forgo at least a like amount. As this needed amending the Act, matters had to wait till April, 1962, when Sec. 35A was introduced to provide for the creation of a Special Reserve Fund. But we saw earlier that response from the States has not been encouraging.

VI.17. Even if all States agree to forgo dividends to the full extent to which Reserve Bank is prepared to make this sacrifice, it would take an average of about 9 years to accumulate upto 10% of the paid-up capital in this Fund. It was seen above (Table IV in Chapter III) that if the States forgo the entire dividends due to them, this period would be reduced to about 5 years. Apart from the fact that accumulation in this Fund would be held down by virtue of the 10% ceiling, as long as post-tax profits cannot meet the total dividend liability, SFCs would continue to draw subvention to accumulate this Special Fund.

VI.18. This situation can perhaps be met in one of these three ways:

(*a*) The States may meet the short-fall of profits (after paying taxes) to pay dividends by an outright grant and not a repayable subvention. (The use of the word "subvention" for such a loan seems inappropriate; its dictionary meaning is a grant of money in aid, or a subsidy). In the last two years, the subvention has averaged at Rs. 16 lakhs, and perhaps in a few years, it will go down substantially. While this method would prevent a further accumulation of subvention liability which is a charge on SFCs' future profits, it would do nothing to correct the present position, viz., the accumulation of SFCs' reserves at a snail's pace.

(*b*) Alternatively, at least for some time the two major shareholders, viz., the States and Reserve Bank, may relinquish all dividends rather than draw them by enhancing the subvention liability, and return a part for the Special Reserve Fund. On the 46.3% and 17.5% holdings by these two holders respectively, they are entitled to dividends of approximately Rs. 22.9 lakhs and Rs. 8.7 lakhs or Rs. 31.6 lakhs annually. At present SFCs pay this sum and can get back upto Rs. 17.4 lakhs for the Special Reserve Fund, if all States contribute as much as Reserve Bank. If these two holders draw no dividends, SFCs would require no subvention and will also receive no contribution to the Special Reserve Fund of Rs. 17.4 lakhs. Thus, under this proposal SFCs would be able to add to the reserves annually Rs. 14.2 lakhs (Rs. 31.6 lakhs minus Rs. 17.4 lakhs). This will mean less credit to the reserves but no accumulation of subvention liability.

States would lose dividends of Rs. 22.9 lakhs; but if subvention payments (about Rs. 16 lakhs) and contribution to the Special Reserve Fund (Rs. 8.7 lakhs) are deducted, there would be a net gain of about Rs. 2 lakhs. This scheme would, additionally, facilitate offering slightly higher dividends to other shareholders to induce them to subscribe to these shares. These institutions would need to strengthen their share capital base in the near future in order to develop fully the various facets of development banking—viz., term lending, guaranteeing, underwriting and also perhaps make small beginnings with direct subscription to the equity of borrowing concerns.

(*c*) The third alternative appears to be the most beneficial to SFCs and also does not involve much loss of tax to Government, if at all.

Since the shares of SFCs carry a guaranteed dividend, this liability is, for all practical purposes, analogous to an element of cost; whatever financial or accounting procedures might dictate, this should be a charge on profits, for as long as the guarantee subsists. To exempt from tax that part of the gross profits which is required for dividends would mean a loss of tax revenue to Government, but it is only a logical concomitant of the scheme of guaranteed dividends. Such a step should have been taken when these institutions were set up. As, however, over a decade has since elapsed, and a few SFCs are now able to meet their dividend liability without recourse to subventions, the Group is suggesting instead a variant of this concession which would benefit the Corporations as well as not involve Government in a loss of revenue more than what they have already agreed to bear under the Finance Act of 1961.

Tax or other comparable concession has been enjoyed by many foreign development banks from their inception. SFCs in India received such a concession only in 1961 to the extent of 10% of their annual profits. We have seen above that even on the very favourable assumption that SFCs' profits continue to increase at the same rate as during 1960-63, the average number of years which the more favourably placed SFCs would take to accumulate upto their paid-up capital in the Special Reserve Account would be about three decades. We suggest, therefore, that 25% of the gross profits of each of these institutions every year should bear no tax and be credited to the Special Reserve Account till such credits add up to the paid-up capital. This measure will promote a somewhat faster growth of reserves than in the existing situation in view also of another factor. The present subvention liability to the States being a charge on the future profits of SFCs, it is very desirable to end this anomalous situation in which the States and Reserve Bank draw dividends out of subventions. If the proposed tax concession is given, not many SFCs would need to draw further subventions.

VI.19. In spite of these considerations in support of the above suggestion, it may be held that it involves giving SFCs a special treatment. It has been shown already that in the case of ICICI and Agricultural Refinance Corporation, special treatment of a different nature has been afforded, in the shape of large long term interest-free loans. In the case of RCI also a sum of as much as Rs. 26 crores has been committed by Government on an interest of only 4%, with the added proviso of paying lower rates in the earlier years. Also, in so far as the SFCs' resources are being directed to the sector of small scale industries as a part of national policy to foster the development of this sector, they are entitled to some concession to build up adequate reserves. Thirdly, development banking in the milieu of an under-developed region needs some stimuli; we are only suggesting to make amends after a decade of neglect.

VI.20. Since under these proposals the States and Reserve Bank will

receive dividends on their shares, they would also continue to forgo such dividends and contribute to the Special Reserve Fund. It was argued in Chapter III that the present ceiling of accumulations in the Special Reserve Fund built out of dividends forgone by these two major shareholders, viz., 10% of the paid-up capital of a SFC, is too low, and may be increased to at least 25% of the paid-up capital. This can be achieved either by retaining the present rates of contribution but continuing it for a longer period to reach this 25% figure, or by increasing the rate of contribution and arriving at the ceiling earlier. Since under the scheme of tax concessions suggested here few State Governments would any longer need to advance subvention to any SFC, they may forgo the entire dividend accruing to them for a limited period rather than limit their contribution to what is forgone by Reserve Bank. Even now a State like Mysore is forgoing more than the Bank. An accumulation of 25% in this Fund would even then take some 12 to 15 years to be reached.

VI.21. One can maintain that as far as SFCs are concerned *the States have made no financial sacrifice beyond perhaps the loss of interest on the amounts advanced as subvention.* SFCs have a pivotal role to play in promoting industrial growth in the medium and small scale sectors. States can very justifiably be called upon now to make some effective contribution towards building up these developmental institutions. There are already other sectors for which they are making a sizable contribution e.g., the co-operative credit institutions. Since 1956-57, i.e. after Reserve Bank set up the National Agricultural Credit (Long-term Operations) Fund, very substantial amounts have been lent from this Fund to the States to enable them to take up shares in such credit institutions. The Bank too has been generous in giving these loans at concessional rates:—for the first two years—0%; next 3 years —2%; next 4 years—2½%; next 3 years—3%. The average rate for the 12-year period is only 1.9%. In most cases, it has persuaded the States that when they take up shares in co-operatives out of these funds, no stipulation is made regarding any dividend; it has also succeeded in preventing the attempt by some States to realise from the beneficiary institutions some returns which are not more than what these Governments have to pay to the Bank. The States are thus shareholders in these institutions, without the guarantee of any minimum dividend.

VI.22. The above measures are expected to strengthen the financial position of these institutions in the years that lie ahead. But they leave unresolved the problem of the *existing subvention liability* of Rs. 1.62 crores. If this is to be a charge on future profits, the likely benefits from the other concessions will be largely wiped out. There seems, therefore, no way of dealing with this last problem except by the simple process of writing off this liability. It may be mentioned that to ICICI, a non-Government undertaking, meant particularly for the large scale sector of Indian industry, Government made a very

generous gesture—an interest-free loan of no less than Rs. 7½ crores, repayable over 15 years, after the expiry of 15 years from drawal. In effect, at a notional rate of interest of 4½% per annum (Government have also given the Corporation a second loan of Rs. 10 crores at 4½% repayable over 10 years beginning from the 11th year), Government is giving a subsidy of Rs. 7.6 crores on this loan over its entire life-span of 30 years. The newly set-up Agricultural Refinance Corporation has also been granted an interest-free loan of Rs. 5 crores by the Central Government, repayable in 15 equal annual instalments commencing after expiry of 15 years from the date of receipt of the loan. SFCs are equally, if not more, deserving of support. It is possible to build a convincing case for such interest-free or low interest bearing loans to SFCs as well. But this is not being done both in view of the other concessions suggested and the large amount that would be needed for all the Corporations, at even Rs. 1 crore for each of them.

Audit & Inspection by Government, private auditors and Reserve Bank

VI.23. Under Sec. 37(1) of the Act, the affairs of a SFC shall be audited by not less than two auditors, one of whom shall be appointed by the State Government in consultation with the Comptroller & Auditor General of India, and the other auditor or auditors elected in the prescribed manner by the shareholders, other than the State Government and Reserve Bank. The Act also provides that the auditors shall make a report to the shareholders upon the annual balance sheet and accounts [Section 37(3)] and that the State Government may, in consultation with the Comptroller and Auditor General, issue directions to the auditors requiring them to report to it upon the adequacy of measures taken by a SFC to protect its shareholders and creditors or upon the sufficiency of their procedure in auditing the affairs of the Corporation and may enlarge or extend the scope of the audit, etc. [Section 37(4)]. Sec. 37(5) makes it incumbent upon SFCs to send a copy of every report of the auditors to the Comptroller and Auditor General at least one month before it is placed before the shareholders.

VI.24. Sec. 37(6) provides that, in addition to these two audits, the Comptroller and Auditor General may, either of his own motion or on a request received from the State Government, undertake such audit and at such times as he may consider necessary; action under the Section is obligatory "where the State Government is required to make any payment on account of the guarantee given by it" for repayment of principal of share capital and payment of annual dividend (under Sec. 6 of the SFCs Act) and repayment of principal and payment of interest on bonds and debentures issued and deposits accepted by the Corporation (under Sections 7 and 8). Every audit report of the Auditor General shall be forwarded to the State Government, and the Government shall cause it to be laid before the State legislature [Section 37(7)]. Since it is only recently that a few SFCs are not drawing subventions from the

State Governments to meet the guaranteed dividend liability, all SFCs have been subject to audit by the Auditor General.

VI.25. Some complaints have been received regarding multiplicity of audits. Kerala SFC, in its reply to the Questionnaire, considers the present system of audit by three different sets of auditors as unnecessary, as the auditors anticipate each other and repeat all possible objections; time that can be utilised for normal and developmental activities has now to be diverted to attend to the audit parties, and adequately answer points raised by them. It has thus been suggested that the State Government should normally be satisfied with the annual audit by the commercial auditors. The nominee of the Comptroller and Auditor General should take up audit only under special circumstances and on specific instructions from the State Government. If this cannot be accepted, the SFC feels that there should at least be some co-ordination between the scope and functions of the different auditors, so that the Corporation has to deal with only one audit report and that too along with the publication of the annual report and thereby the Corporation's workload could be reduced. Madhya Pradesh Corporation also does not favour the present system of multiplicity of audit on similar grounds and has suggested that the number of audits and inspection might be reduced to two, viz., audit by the public auditors or by the Auditor General, and inspection by Reserve Bank.

VI.26. A proposal to amend Sec. 37 of the SFCs Act for dispensing with the provision for appointment of an auditor by the State Government and for making the audit by the Comptroller and Auditor General compulsory every year was considered by the Seventh SFCs' Conference held in December, 1960. The Conference, however, felt that it was good in principle to have two auditors; the difficulties experienced by the Corporations on account of dual audit could be avoided by bringing about synchronisation of audit by the auditors or sharing of the work as might be considered convenient. But such synchronisation and/or sharing may not be sufficiently feasible to give the measure of relief sought by the Corporations, as each audit party would like to do a complete job. It is for consideration if the State Governments may not waive their right to appoint an auditor, and be satisfied with the audits (*i*) by the auditor appointed by shareholders other than the State Governments and Reserve Bank, and (*ii*) by the Auditor General till such time as this is done statutorily under Sec. 37(6). When the latter audit ceases and any State Government has special reasons for wanting an audit in addition to the one conducted by the auditor appointed by the other shareholders, it may request the Auditor General to undertake an audit under Sec. 37(6). This will require the existing Sec. 37(1) to be amended.

VI.27. These considerations relate to audit, and do not affect the necessity for a systematic and periodical inspection of SFCs. The scope of inspection is much wider than that of audit, and its purpose is not

so much to verify the accuracy of financial transactions or to ascertain whether the sanction of the competent authority has been obtained for a particular expenditure or disbursement, but to concentrate on policy matters e.g., the soundness, judged by financial standards, of the investments made or loans sanctioned by a Corporation and whether the trend of advances made is in general keeping with the policy of Government and Reserve Bank.

VI. 28. Besides, being an impartial and independent agency, Reserve Bank, as the central banking institution of the country. has acquired considerable experience in the inspection of both commercial and co-operative banks and is in a unique position to conduct periodical inspections of SFCs as well. The proposal that Reserve Bank should statutorily inspect SFCs periodically was endorsed by the representatives of most of the Corporations at the first SFCs' Conference held in August, 1954. To empower the Bank to conduct such inspections, the SFCs Act was amended in 1956.

VI.29. Table XV, indicating the inspections conducted so far by Reserve Bank, will show that the Bank has already inspected all Corporations at least once except the Jammu & Kashmir SFC which has been recently set up and has so far transacted only a small amount of business. While SFCs in five States, viz., Andhra Pradesh, Kerala, Maharashtra, Uttar Pradesh and West Bengal have been covered by three rounds of inspection, those in the States of Assam, Bihar, Madhya Pradesh, Mysore, Punjab, Orissa and Rajasthan have been inspected twice. The Corporations of Gujarat and Madras have been inspected only once so far. Gujarat SFC was established only in May, 1960 and Madras Corporation was brought under Sec. 37(A) of the Act (as also Sec. 38 relating to "Returns") in 1961. These inspections should be carried out at least biennially. To make these inspections more constructive, it is suggested that their scope may be enlarged to examine how far the Corporations are performing the various functions for which they were set up and those which are called for in the context of a policy of rapid industrialisation.

Management of State Financial Corporations

VI.30. In terms of Sec. 9 of the Act, the general superintendence, direction and management of a SFC shall vest in a Board of Directors which, with the assistance of an Executive Committee and a Managing Director, may exercise all the powers and discharge all the functions which may be exercised or discharged by the Financial Corporation. Sec. 10 provides for the creation of the Board, to consist of ten directors—five nominated, four elected, and a Managing Director—as follows: —

(*a*) three nominated by the State Government and (*b*) one each nominated by the Reserve Bank of India and the Industrial Finance Corporation of India; (*c*) three directors elected in the prescribed manner by the parties, one each to represent scheduled banks,

TABLE XV

Statement showing the details of inspections of State Financial Corporations conducted by the Reserve Bank of India upto March, 1963.

Sl. No.	Corporation of	Frequency of inspections	Period during which the inspection was carried out		
			First inspection	Second inspection	Third inspection
1.	Andhra Pradesh	Three	Aug.-Sept. 1957	Jan.-Mar. 1960	Dec. 1962-Feb. 1963
2.	Assam	Two	Apr. 1958	June-July 1960	—
3.	Bhiar	Two	Dec. 1957	Aug.-Sept. 1960	—
4.	Maharashtra	Three	Aug.-Sept. 1956	Aug.-Oct. 1959	June-Aug. 1962
5.	Gujarat	One	Dec. 1961-Jan. 1962	—	—
6.	Kerala	Three	Mar.-Apr. 1957	June-July 1959	May-June 1962
7.	Madhya Pradesh	Two	Aug. 1958	Oct. 1961	—
8.	Madras	One	Aug.-Oct. 1961	—	—
9.	Mysore	Two	June 1961	Jan.-Feb. 1963	—
10.	Orissa	Two	Jan. 1960	Oct.-Nov. 1962	—
11.	Punjab	Two	Sept.-Oct. 1957	May 1960	—
12.	Rajasthan	Two	Oct.-Nov. 1958	Dec. 1961-Jan. 1962	—
13.	Uttar Pradesh	Three	Mar.-Apr. 1957	Mar.-Apr. 1959	Mar. 1962
14.	West Bengal	Three	June-July 1957	Oct.-Nov. 1959	Sept.-Oct. 1962
15.	Jammu & Kashmir	Nil	—	—	—

co-operative banks, and remaining financial institutions, and one director elected by remaining shareholders; (*d*) a managing director appointed by the State Government in consultation with Reserve Bank and, except in the case of first appointment, also with the Board.

VI.31. In terms of Sec. 15(1), the Chairman of the Board shall be one of the directors, not being the Managing Director, nominated by the State Government, after considering, except in the case of the nomination of the first Chairman, the recommendation of the Board. In terms of Sec. 17(1), the Managing Director shall be wholetime officer and hold office for such terms not exceeding four years as the State Government may specify. However, he is eligible for re-appointment. Formerly, the State Governments used to consult Reserve Bank informally in regard to the appointment/extension of the term of office of the Managing Directors. With the amendment of the SFCs Act in 1962, such consultation [Section 10(*f*)] is now a statutory obligation.

VI.32. The nominees of the State Government often include prominent non-officials with business experience, in addition to senior officers like the Finance Secretary, the Director of Industries, etc. The nominee of the Reserve Bank of India is generally either a senior officer of the Bank or a member of one of its four Local Boards. IFC, which till last year nominated its directors to the Boards of these Corporations has now replaced them by its senior officers in most States. The director-nominees may not often find time to study the Board papers or attend the Board meetings of the Corporations. IFC is primus inter pares among the term lending institutions in the country, and it is expected to give guidance and advice to SFCs whenever necessary. This objective would be served best if it nominates only its senior officers to SFCs who could also effectively act as intermediaries for informal consultations on such matters as terms and conditions of participation arrangements, underwriting, etc.

VI.33. As a result of certain amendments of the general regulations some time ago, LIC, which can now elect a director under category '(*c*)' above, can ensure a seat on the Board in all SFCs by virtue of the magnitude of its shareholdings. In that case, other financial institutions like insurance companies, non-scheduled banks, investment trusts, etc. will get no representation, while it is necessary that there should be a place for them if the share and bond holdings of SFCs are to be made more broad-based in the future. Provision may therefore be made for an additional director to represent these other financial institutions.

VI.34. At present, four out of fourteen SFCs, viz., those of Gujarat, Maharashtra, Uttar Pradesh and West Bengal, have appointed persons having commercial/co-operative banking experience as their Managing Directors; five Corporations—of Andhra Pradesh, Bihar, Kerala, Mysore and Madhya Pradesh—have Government officials on deputation from the State Governments and two Corporations—of Punjab and Rajasthan, have appointed retired Government Officers with experience of

various executive posts, as their Managing Directors. The Managing Director in Orissa is a Chartered Accountant, with more than five years' experience in the working of Orissa SFC. The Managing Directors in Assam and Jammu & Kashmir are on deputation from the State Bank of India and the Reserve Bank of India respectively. Thus, most of the present Managing Directors are either bankers or Government officials (Appendix II to this Chapter gives the particulars of the present Managing Directors of the Corporations). But experience of commercial banking alone is not adequate as term lending is fast becoming a specialized vocation. No effort has been made so far to give the Managing Directors orientation courses in term lending. It may be useful to explore the possibilities of securing the assistance of the Development Banks Services Department of the International Finance Corporation in this regard. The average age of the present Managing Directors is 53; Corporations may try to secure younger men who would also have a longer run of employment.

VI.35. The Chairman of a SFC shall hold office for two years or until his successor is nominated [Sec. 15(2)]. He is eligible for re-appointment. In most SFCs, the Chairmen are generally prominent businessmen or industrialists. In Punjab and Jammu & Kashmir, Government Officials belonging to the IAS cadre are now Chairmen. In the case of the following seven SFCs, there has been no change in the incumbency of the Chairman since their inception:—Assam, since 1954; Bihar, since 1954; Madhya Pradesh, since 1955; Rajasthan, since 1955; Maharashtra, since 1956; Andhra Pradesh, since 1956; and Gujarat, since 1960. In West Bengal, the first Chairman held office for over nine years i.e. upto August, 1963. In Kerala, the first Chairman held office for four years and the present Chairman is holding the post for the past six years, while the tenure of office of the Chairmen of Uttar Pradesh and Punjab Corporations ranged between two and four years. The first Chairman of Mysore Corporation (a Government official) held office for one year and the second Chairman is in office since 1960. In the case of Orissa, the first Chairman was in office for four years and, thereafter, there was a change in the incumbency of the Chairman almost every year. The first Chairman of Jammu & Kashmir Corporation remained in office for one year only and the present one is in office since 1961.

VI.36. In Kerala, West Bengal and Rajasthan, the Managing Directors held office for four to seven years and in Punjab, Maharashtra, Jammu & Kashmir, Assam, Orissa and Bihar, their tenure ranged between two and four years. In Andhra Pradesh and to some extent in Madhya Pradesh, Managing Directors changed annually with the exception of one incumbent each, who held office for four years. In Uttar Pradesh, the first Managing Director's term was two years; his successor remained for five years. In Gujarat, the term of office of the first Managing Director was extended year by year and he held the post

for nearly three years while in Mysore, none of the first three Managing Directors remained in office for more than a year and a half. This frequent change is admittedly harmful to the Corporation, as the employee concerned does not feel the same stake in the institution as he would have if a more continuous employment were assured for him.

VI.37. As the Chief Executive, the main work devolving on the Managing Director is to invest and lend the Corporation's funds and to augment them from time to time according to need. He is also, by statute, Chairman of the Executive Committee. He should, therefore, be a person with requisite experience, particularly in the now admittedly technical matter of granting term loans. The exercise of adequate vigilance after funds have been invested or lent also calls for training and experience, which a person who has held a responsible position in a lending institution would have presumably acquired. Perhaps persons on deputation from the State Government (or State Bank) may not feel the same stake in the fortunes of the Corporations as a permanent employee would, as the former, being liable to be transferred according to exigencies of their service, may not have a sufficiently long innings in the Corporations to be able, or even willing, to formulate and implement sound policies which will only bear fruit over a period of time. In the circumstances, it is not advisable to appoint Government officials to these posts on a deputation basis unless they are adequately qualified for the job they have to handle and can be left undisturbed for at least four years; otherwise, suitably qualified outsiders may be appointed as permanent employees of the Corporations.

VI.38. In terms of Sec. 18(1) of the Act, the Executive Committee shall consist of the Managing Director, as its Chairman, and three other directors—one from among the directors nominated by the State Government, one out of the two directors nominated by Reserve Bank and IFC, and one of the elected directors. In the case of Joint Financial Corporations, the Executive Committee shall in addition consist of as many Government nominated directors as there are participating States. Sec. 20 of the Act provides that, subject to such general or special directions as the Board may from time to time give, the Executive Committee may deal with any matter within the competence of the Board. In terms of sub-section (2) of this Section, the minutes of every meeting of the Executive Committee shall be laid before the Board at the next following meeting of the Board. All SFCs have set up Executive Committees. The Executive Committees of only six SFCs—Assam, Bihar, Maharashtra, Mysore, Rajasthan and Uttar Pradesh—have been empowered to dispose of loan applications upto Rs. 1 lakh while those of Gujarat, Madhya Pradesh and Punjab have been empowered to grant loans upto Rs. 2 lakhs. The rest have as yet no sanctioning powers but only screen applications, and make recommendations to the Board. The executive Committee of Kerala SFC is, however, authorised to finally

dispose of applications under the agency arrangement with the Government. For this purpose, two State Government representatives also participate.

VI.39. In the case of those SFCs whose Executive Committees have not been empowered to sanction loans, there is likely to be delay in disposal of applications as all will have to be disposed of by the Board which meets less often than the Executive Committee. It will, therefore, be advisable for the Boards of these SFCs to delegate to their Executive Committees power of sanctioning loans upto Rs. 2 lakhs in each case as is the practice in Punjab SFC.

VI.40. Sec. 21 of the Act provides for the appointment of one or more Advisory Committees to assist the Corporation in the efficient discharge of its functions, especially for securing that those functions are exercised with due regard to the circumstances and conditions prevailing in, and the requirements of, particular areas or industries. But SFCs of Andhra Pradesh, Bihar, Gujarat, Jammu & Kashmir, Mysore, Orissa, Rajasthan and Uttar Pradesh have not yet set up Advisory Committees. These Committees generally consist of some directors of the Corporations and a few representatives of industry in the State. In Assam, there is a Tea Advisory Committee to advise on the general policy regarding the sanction of loans to tea gardens and to give technical advice and carry out inspection and valuation. There is also a Tripura Advisory Committee to advise in the matter of sanctioning loans to concerns situated in Tripura. Kerala Corporation is unique in having set up Regional Advisory Committees in five out of the nine revenue districts, to give detailed information to local parties on the functions of the Corporation and the procedure for obtaining assistance from it. Maharashtra Corporation has no Standing Advisory Committee, but whenever necessary the Board sets up ad hoc Committees for technical and other advice. The Punjab Corporation has at present Advisory Committees for (*i*) General engineering; (*ii*) Textiles, including hosiery; (*iii*) Cold storage; and (*iv*) Electricity supply undertakings. It has also panels for Transport and Hotel industries, on which concerned State Government officials are also invited to serve. The functions of these Advisory Committees include examination of applications referred to them for technical advice and opinion about the scope of the industry and extent of requirement of finance of the applicants. West Bengal Corporation has recently set up an Advisory Committee for North Bengal which is largely experimental and as such has not been allotted any specific functions. Appendix III to this Chapter shows the dates of constitution, composition and functions of the Executive and Advisory Committees of various SFCs.

VI.41. As regards trained staff, six SFCs—in Bihar, Kerala, Madhya Pradesh, Maharashtra, Rajasthan and Uttar Pradesh—have already sent one or more of their officers for study and training at the Industrial Finance Course run by the Bankers Training College of Reserve

Bank. All the Corporations have at least some officers who have had training in banking or accountancy. The officers of Punjab Corporation are stated to be adequately qualified and experienced. Maharashtra Corporation claims to have adequate staff. In Gujarat and West Bengal, the staff position is stated to be not satisfactory.

VI.42. The availability of technical advice (and creation of panels of technical experts, etc.) has been reviewed at many of the SFCs' Conferences. In pursuance of a decision taken at the 6th Conference held in 1959, Reserve Bank had examined the whole question regarding the nature of technical advice being obtained by the Corporations and their actual requirements. The Corporations were advised, among other things, that it would be advantageous for them to have at least one technically qualified person on their permanent staff (with general knowledge of engineering and particular knowledge of one or two industries predominant in the area of operation of the Corporations). The present position of the technical facilities availed of by the Corporations together with their opinion in this respect are briefly indicated below.

VI.43. Regarding technical consultations for scrutiny of loan applications, five Corporations—in Assam, Madras, Maharashtra, Mysore and Uttar Pradesh—hold that the present arrangements for technical appraisal are satisfactory. Assam and Maharashtra SFCs refer schemes to the Directorate of Industries and Small Industries Service Institutes for technical scrutiny, while Madras Corporation utilises the services of technical staff employed in various industrial units, for the purpose. Mysore Corporation has engaged one full-time engineer and, in addition, three part-time technical advisers holding responsible posts in Government. Uttar Pradesh Corporation has a technical officer of its own, and experts from the Directorate of Industries, National Sugar Institute, Small Industries Service Institute and SFC's panel of advisers are consulted for technical appraisal of schemes. Altogether five Corporations—of Andhra Pradesh, Mysore, Madhya Pradesh, Orissa and Uttar Pradesh—have engaged technical persons like mechanical or industrial engineers on their staff. Seven Corporations—in Assam, Bihar, Gujarat, Kerala, Maharashtra, Orissa and Uttar Pradesh—are consulting the Directors of Industries in their States for obtaining technical reports; Kerala Corporation consults the Director of Industries only for applications from small scale units. The Corporations in Rajasthan and West Bengal hold that present arrangements for technical assistance are not satisfactory. Punjab Corporation is of the opinion that the present arrangements, though satisfactory, need improvement. No Corporation consults local Chambers of Commerce and Industry. Some have set up Advisory Committees or panels of technical experts in each industry. Some of the Corporations (Gujarat, Jammu & Kashmir and Orissa) feel that panels of experts for different industries should be set up at State or Central level or a Central Organisation on a regional or zonal basis

for each State or group of States may be set up to make available the services of technical consultants. Again, it has been suggested in some quarters (Orissa Government) that as SFCs cannot afford to engage experts of their own for the purpose of furnishing technical reports, SFCs, SBI, commercial banks (and Directors of Industries) should have a common pool of experts in each State.

VI.44. Most foreign development banks have engaged full-time technical staff of their own, but they operate on a much larger scale than SFCs. We have earlier referred to the definitive views of the "Working Group on Appraisal of Applications for Term Loans" in the matter of requirements of technical staff of term lending agencies, viz., that each lending institution should have a minimum complement of one team consisting of trained and experienced persons from each of the three fields—engineering, industrial economics and accounting—at a fairly senior level.

VI.45. Though this is an ideal to be aimed at by all SFCs, some of them may find the cost of engaging a complement of technical staff more than their present volume of operations would justify. It would, therefore, be necessary to devise some means by which their requirements in this direction could be met; and it is suggested that a list of engineers/accountants serving in different industries within the jurisdiction of each SFC and willing to tender advice on technical problems may be drawn up and applications referred to them for scrutiny and advice on payment of fees on a scale to be fixed in advance. As there is dearth of experienced technical personnel in the country, this avenue is worth exploring. Another possibility which might be examined is the setting up of an independent technical and economic evaluation institution with branches in important business centres which could serve the evaluation needs of not only SFCs but other lending agencies like IFC, ICICI, commercial banks, etc. Banks have in recent years taken to term lending significantly and they will be called upon to expand this type of business to meet the requirements of their ever-increasing industrial clients. Like SFCs, they would also require the services of competent technical staff and the proposed evaluation institution would, if it operates on a large scale, be able to quote reasonable rates for its services.

VI.46. In the matter of post-sanction utilisation of loans granted, twelve SFCs obtain progress reports in prescribed forms which generally contain data regarding (1) value of security (2) utilisation of loan (3) implementation of scheme (4) quantum of production and sales and (5) employment. These details enable the Corporations to maintain post-disbursement checks on the loans granted. Reserve Bank circulated (in January, 1960) to all the Corporations model forms of progress, first inspection and post-disbursement inspection reports for their guidance. The forms prescribed by the Bank are under consideration of Jammu & Kashmir Corporation, while Mysore Corporation ensures proper

utilisation of loans (except for working capital purposes) by physical inspection or verification of documents, etc. Madras Corporation also obtains periodical returns from marginal units.

VI.47. The importance which the "Working Group on Appraisal of Applications for Term Loans" has bestowed on the follow-up and supervision of loans has already been indicated in an earlier section. But almost all Corporations experience difficulty in getting the data they ask for, as proper accounts are often not maintained by the borrowers, particularly those in the non-corporate sector. Only six Corporations—of Andhra Pradesh, Assam, Gujarat, Maharashtra, Rajasthan and Uttar Pradesh, are of the view that their returns give complete details to watch the utilisation of the loans. Madhya Pradesh Corporation does not concur with this, and it verifies utilisation by checking original vouchers and physically inspecting assets of the concerns. According to Orissa Corporation, the returns, if furnished regularly, would give sufficient information ; as they are not supplied regularly, the Corporation checks utilisation before further disbursements. While Punjab Corporation obtains additional exhaustive data during the course of post-sanction inspections, Bihar Corporation checks utilisation of loans at the time of post-disbursement inspection. Kerala Corporation considers that the reports of inspectors are sufficient for the purpose. West Bengal Corporation is of the view that the data called for, if supplied, are sufficient. However, in the absence of progress reports, utilisation of funds is watched from balance sheets in most cases.

VI.48. All the Corporations undertake inspections of the units financed by them generally on a yearly or half-yearly basis ; some of them with special inspection staff.

VI.49. The Development Finance Corporation of Ceylon, China Development Corporation, Industrial and Mining Development Bank of Iran, Development Bank of Philippines and Pakistan Industrial Credit and Investment Corporation inspect the units, both before and after sanction of the loan. The Western Region Finance Corporation of Nigeria conducts inspection prior to granting loans. All the above foreign development banks (except Nigeria) undertake loan supervision or follow-up surveys and obtain periodical returns.

VI.50. It has been already stressed in Chapter IV above, that, in the context of the planned economic development that is being attempted through the Five Year Plans, it will be necessary for each SFC to become more and more what a development bank should be in a relatively underdeveloped economy. They will have to take a keener interest in new ventures and assist would-be entrepreneurs in the preparation of suitable projects, especially in relation to their financial and commercial aspects, so as to be able to launch such prospective industrialists on a career in industry. It would also be worthwhile for SFCs to be associated with Governmental and other agencies which undertake research or surveys, with a view to uncovering fresh investment opportunities within

their areas of operation. In this connection, mention may be made of the proposal of Rajasthan Financial Corporation to set up a 'cell', with a senior officer and a statistician, to assist and guide intending industrialists. The cell is proposed to make a continuous study of the possibilities of industrial development in the State, prepare concrete schemes, guide entrepreneurs and maintain liaison with the concerned State and Central Government departments and other institutions concerned with industry. As the development of industry is the responsibility of the State Government and this cell would be engaged in a primarily promotional activity, the Corporation has suggested that three-quarters of the cost may be met by the State Government. It is understood that no final decision has been taken regarding this proposal. State Financial Corporations and State Governments elsewhere may also consider this suggestion.

VI.51. The provision of finance cannot be the only function of SFCs. Entrepreneurs may need technical advice to prepare and execute projects and for their management. Such advice does not end with the working out of a project and providing the necessary funds. It will have to continue during the tenure of the loan, as new problems and difficulties emerge. This underlines again the need for SFCs to build up a complement of technical and advisory staff in due course which would be of mutual advantage to SFCs as well as the business community. Unless such steps are taken, SFCs will fairly consistently reject applications from small enterprises and confine their operations to the larger units, the applications of which are usually a product of detailed study and greater experience.

VI.52. Further, SFCs are normally expected to restrict their assistance to types and maturities of financing which other lending institutions like banks are not prepared to undertake. Their management must thus appreciate that SFCs are development banks, and exist to take risks which others are unfitted to assume; and also that there will certainly be some loss in their operations from time to time. Losses could, of course, be avoided by accepting only first class business but if they are to fulfil the expectations entertained of them, they will have to assume risks. Their management must, therefore, have a combination of good judgement and imagination and strike the balance between excess caution and excess risk taking. The Group has already given its recommendations regarding strengthening the finances of SFCs with a view to enabling them to take the necessary calculated risks of development banking.

VI.53. In this connection, we may refer to a suggestion that is sometimes made that a SFC which always has its office in the State capital should have one or two branches in other parts of the State. This would familiarise the people with its operations and expedite the flow of business. A decision on this matter should really be guided by the merits of each case. Publicity is undoubtedly an important activity and SFCs

should take necessary steps to this end. As for branches, since the power of sanction of loans must vest in the Board/Executive Committee which sits at the headquarters, branches can only act as an effective liaison with local business community. Before any branch is set up, two other things may be done—agency arrangements may be entered into with branches of the State Bank of India at selected centres to receive applications as well as collect further data from borrowers; secondly, at those selected centres, small Advisory Committees may be set up to give their views to the Board regarding proposals emanating from those centres. The practice of some SFCs holding their Board meetings at different centres in the States may also be adopted by others. If it is found after some time that the volume of business at any one of these selected centres has assumed handsome proportions, the question of setting up small branches there may be considered.

VI.54. There is another matter, viz., maintenance of statistics by SFCs which deserves attention. At present SFCs are submitting certain periodical returns to the Reserve Bank of India, the performance for which have been recently revised. Both before, and particularly in connection with supplying certain data to this Working Group, the need for a small statistical cell in each SFC has become evident. The cell need consist of only one or two people responsible directly to the Managing Director. As the operations of each SFC gain momentum, it will be increasingly necessary for them to maintain detailed statistics to help the Board in assessing the progress of the institutions and finding out where gaps lie.

VI.55. It was indicated earlier that the Corporations have much difficulty in getting financial and other data from the applicants, as well as such minimum information as is needed to assess the progress of borrowing concerns. This difficulty arises specially for non-corporate concerns where accounting procedures are still not standardised according to the double entry method which is adopted by corporate units. This is, of course, a problem common to the entire sector of small scale units. In March, 1962, Reserve Bank devised a set of simple forms of statements for such units and forwarded them to the Small Scale Industries Board for its consideration. The matter came up at the 10th and 11th meetings of the Committee on Credit Facilities that year when a Sub-Committee was appointed to examine these forms. The Sub-Committee recommended a minimum set of books of accounts but no action on the lines suggested by the Bank seems to have been taken by Government. It is recommended that Government may try out these forms on a 'pilot' basis in selected areas, and then prescribe them for adoption. They may, in due course, make it obligatory for units seeking assistance either from the Government under the State Aid to Industries Act, or from SFCs or from NSIC, to maintain certain minimum accounts on standardised patterns, and submit such information as may be required to process their applications, and assess the progress made by them

from time to time. This is an essential part of any plan to develop the industrial sector on rational lines.

K. C. Mittra
Chairman
Bharat Bhushan
B. K. Chatterjee
B. K. Chatterji
N. M. Chokshi
M. Narasimham
J. S. Raj
C. A. Subrahmanyam
S. R. Varma
A. K. Banerji
Member-Secretary

Bombay,
6th February, 1964.

Appendix I to Chapter VI

Fiscal Concessions to Development Banks in Some Foreign Countries

In view of the special role assigned to development banks in promoting rapid industrial development and to enable them to buttress their resources and build up adequate reserves, these institutions in some foreign countries have been given tax concessions while, in other cases, their earning-potential has been enhanced by the Government providing substantial interest-free, or low interest-bearing, funds to be utilised for their business. Details of some of these fiscal concessions and other benefits are given below:

(i) Tax concessions

The Government Development Bank for Puerto Rico and the Western Region Finance Corporation, Nigeria, are exempt from taxation. The Uganda Credit and Savings Bank, which grants industrial loans, is also wholly exempt from income tax. Income tax is not also applicable to the Japan Development Bank on a permanent basis. Though the above institutions are State-owned, others, viz., the Industrial and Mining Development Bank of Iran, the Pakistan Industrial Credit and Investment Corporation and the Industrial Development Bank of Pakistan, which are privately-owned or mixed ventures, also enjoy certain tax concessions. While the net profits of the Iranian institution are exempt from income tax upto a maximum of 6% of the bank's paid-up capital and the interest-free advance from the Government, viz., Rials 400 million and Rials 600 million respectively, in the case of the Pakistan development banks, upto 10% of their annual income (to be credited to Special Reserves) is tax-free. According to the provisions of Iranian commercial law, the Industrial Guarantee Fund of Iran which is a non-Governmental non-profit organisation, however, is wholly exempt from taxes. Besides, in terms of its Charter, all sums due to the Industrial Development Bank of Pakistan are recoverable as arrears of land revenue, a privilege not enjoyed, at present, by State Financial Corporations in India.

(ii) Interest-free or low interest-bearing loans

In addition to tax concessions, some development banks have also received from their Governments, loans which are mostly interest-free and/or bear low interest rates. The position regarding these and other banks is as follows:

(*a*) Industrial and Mining Development Bank of Iran

The bank has received loan from the Government of Rials 600 million, referred to earlier. This loan, which is for 30 years, is *interest-free.*

(*b*) Pakistan Industrial Credit and Investment Corporation

It has received two loans of Rs. 30 million each, one for 7½ years *free of interest* and the other at 4% for 36½ years.

(*c*) Industrial Development Bank of Pakistan

This bank has been granted low interest bearing loans to the extent of Rs. 5.14 crores as under.

	Amount (Rs. crores)	%	Rate of Interest %
	1.75	34.0	2
	1.00	19.5	3½
	1.90	37.0	4
	0.49	9.5	4½
Total	5.14	100.0	—

(*d*) Western Region Finance Corporation, Nigeria

Loans received from the Government aggregate £2.47 million, of which £0.55 million are at 3½% interest and the balance at 5%.

(*e*) The Industrial Guarantee Fund of Iran

The Fund has made arrangements with the Plan Organisation of the Government for a loan of Rials 800 million at 2½%.

(*iii*) *Development banks in certain other countries, though subject to tax, are nevertheless in receipt of loan assistance from the State.*

(*a*) Development Finance Corporation of Ceylon

Though privately-owned, this institution has received from the Government, loans amounting to Rs. 16 million, which are *interest-free* and are repayable in 15 equal annual instalments, the first being due in the 16th year after grant of such loan.

(*b*) China Development Corporation, Taiwan

This Corporation (which is a mixed concern, with its stocks predominantly owned by private investors), is in receipt of loans from the Government at 6% for 30 years, with amortisation beginning from the 16th year. Total amount obtained is N.T. $300 million.

(c) Development Bank of the Philippines

Loans have been granted by Government at 0% to 2% for various periods. The bank has also received loans from the Central Bank of the country at 1% to 3%. This institution is State-owned.

(iv) *Liability to pay guaranteed dividend*

Five State-owned foreign development banks, viz., Government Development Bank for Puerto Rico, Development Bank of the Philippines, Uganda Development Corporation, Japan Development Bank and Western Region Finance Corporation, Nigeria, are *not* required to pay any dividend. The Industrial and Mining Development Bank of Iran, Development Finance Corporation of Ceylon, Pakistan Industrial Credit and Investment Corporation and China Development Corporation, which are mostly private institutions and which declare dividends, are *not,* however, burdened with the liability of paying a minimum guaranteed dividend, as in the case of State Financial Corporations. In fact, some of them did not pay dividends for some years e.g., Development Finance Corporation of Ceylon for three years, and China Development Corporation and Pakistan Industrial Credit and Investment Corporation for one year. Except in the case of one privately-owned institution, i.e. Industrial Development Bank of Turkey, a dividend of 6% was guaranteed by the Government only in the first three years of the bank's working and actually dividend for the first year was paid out of a special loan from the Government.

It will be seen, therefore, that development banks in many foreign countries are in receipt of tax incentives. Even those which do not enjoy such concessions nevertheless get other benefits from the State in the form of interest-free/low interest-bearing loans. By and large, they are also not saddled with the liability of paying a minimum guaranteed dividend.

APPENDIX II TO CHAPTER VI

PARTICULARS OF PRESENT MANAGING DIRECTORS OF STATE FINANCIAL CORPORATIONS

1. *Punjab Financial Corporation :* Shri S. R. Varma, M.A., I.A.S., (Retd.) was appointed on 8th April, 1959, for four years in the scale of Rs. 1400-100-1900. His term was later extended for two more years upto 7th April, 1965. He is 59 years old. He worked as Excise and Taxation Commissioner, and Finance Secretary and Planning Development Commissioner, Government of Punjab. As Finance Secretary, he was Chairman of the Corporation from February, 1957 to July, 1958.

2. *Kerala Financial Corporation :* Shri M. G. Achyuthan Nair, B.Com., (53 years) was appointed Managing Director on 26th December, 1957 in the scale of Rs. 650-50-1000 plus D.A. (at rate admissible under

the Corporation's rules). He was formerly Commercial Accounts and Audit Officer and Deputy Secretary to the Government of Kerala.

3. *Maharashtra State Financial Corporation :* Shri P. S. Mokashi, B.A., (57 years) was appointed on 14th August, 1962 on Rs. 2000 p.m. in the scale of Rs. 1500-100-2000. He worked as Agent of a branch and Inspector of Societies in the Bombay Provincial Co-operative Bank Ltd. (1928-38) and as General Manager of Sangli Bank (from 1939). He joined Reserve Bank in 1950 and retired as Deputy Chief Officer, Department of Banking Operations.

4. *Andhra Pradesh State Financial Corporation :* Shri O. Swamynatha Reddy, B.Com. (Hons.), A.C.A., (33 years) was appointed on 31st August, 1963 for six months. He had officiated as Managing Director for 13 months in 1961-62. He joined the Corporation in March, 1960 as Secretary-cum-Accountant. Before this, he was Assistant Manager in a private limited company. He draws Rs. 300 p.m. in addition to his emoluments as Secretary-cum-Accountant of Rs. 1193 p.m. (including D.A., House Rent Allowance and Provident Fund).

5. *West Bengal Financial Corporation :* Shri M. K. Adhikari, B.A., C.A.I.B. (London)—62 years—retired Chief Accountant of the State Bank of India, Calcutta, joined as Managing Director on 1st March, 1961. He draws Rs. 2700 p.m. including Rs. 200 as car allowance, in addition to his pension from State Bank.

6. *Assam Financial Corporation :* Shri K. P. Barooah, B.A., (49 years) was appointed on 1st November, 1958. His term was extended for the second time for two years from 1st November, 1962. He draws Rs. 1575 p.m. Before joining the Corporation on 1st November, 1957 as Secretary, he was Agent, State Bank of India, Gauhati, and is on deputation from that bank.

7. *Uttar Pradesh Financial Corporation :* Shri Bharat Bhushan, B.A. (Econ.), C.A.I.B. (London)—58 years—was appointed on 1st November 1961 on one year's probation and was sanctioned continuation for further two years from 1st November, 1962. His pay scale is Rs. 1200-75-1500 p.m. plus pension and D.A. of Rs. 900 from the State Bank of India. He passed the Gilbert Examination in Banking with Honours (1927) and was trained in Midland Bank Ltd., London (1927-28). He was Superintendent, Foreign Exchange Department, Punjab National Bank (1929-31) and worked in the State Bank of India (1931-59). Between 1959-61, he was General Manager, Uttar Pradesh Co-operative Bank Ltd., Lucknow.

8. *Bihar State Financial Corporation :* Shri H. P. Shaw, B.A., (48 years) was appointed on 5th July, 1963 in the grade of Rs. 800-35-1150 plus a special pay of Rs. 150 p.m. Earlier, he was Deputy Commissioner, Commercial Taxes, Government of Bihar. He belongs to the Bihar Financial Service.

9. *Rajasthan Financial Corporation :* Shri G. S. Purohit, I.A.S., (Retd.)—57 years—was appointed on 23rd January, 1961. He draws

Rs. 1423 p.m. plus Rs. 250 as conveyance and entertainment allowance in addition to pension from the Government of Rajasthan. Before retirement from the State Service, he was Financial Commissioner. Earlier, he was Finance Secretary, Jaipur State, and Finance Secretary, Rajasthan, when he was responsible for the organisation of the Bank of Jaipur and represented the State Government on its Board. He also represented the Government on the Board of Rajasthan Financial Corporation.

10. *Madhya Pradesh Financial Corporation :* Shri B. K. Chatterjee, M.Sc., M.A., I.A.S., (55 years) was appointed on 23rd November, 1960, on deputation from the State Government. He draws pay in the senior I.A.S. scale plus a special pay of Rs. 250 p.m. He was Finance Secretary in the former Madhya Bharat (1953-56), Deputy Secretary, Commerce and Industries Department, Madhya Pradesh (1957-59) and Deputy Secretary, Public Works Department, Madhya Pradesh.

11. *Orissa State Financial Corporation :* Shri R. N. Sahoo, B.A., B.Com., C.A. (32 years) was appointed on 1st June, 1959 in the scale of Rs. 500-50-1250 plus D.A. admissible to senior Government employees. He was earlier partner of a firm of Chartered Accountants for one year and joined the Corporation as Accountant on 1st April, 1957. He acted as Managing Director from 7th July, 1958 to the date of his present appointment.

12. *Mysore State Financial Corporation :* Shri C. M. Kempanna, B.Sc. (Hons.), 50 years, was appointed on 7th September, 1961. His pay scale is Rs. 800-1800 (senior I.A.S. scale) plus high price allowance at Central rates and a special pay of Rs. 100 p.m. Earlier, he was Deputy Secretary to Government of Mysore, Planning and Development Department and Deputy Commissioner, Land Records. He was also Secretary, Mysore Chemicals and Fertilisers for five years.

13. *Gujarat State Financial Corporation :* Shri N. H. Shah, B.A., LL.B., C.A.I.I.B., G.D.C.A. (51 years) was appointed on 1st April, 1963 in the scale of Rs. 1200-50-1500 EB. 100-1800 and conveyance allowance Rs. 150 p.m. and house rent allowance @ 7½% of pay. He held various posts in the Bombay Provincial Co-operative Institute, Nadiad, Kaira District Co-operative Land Mortgage Bank, Surat District Co-operative Bank and Gujarat State Co-operative Bank.

14. *Jammu & Kashmir State Financial Corporation :* Shri M. L. Bhalla, B.Sc., (52 years) was appointed on 1st November, 1961 on deputation from Reserve Bank. He draws pay and allowances admissible to him in the Bank plus deputation allowance at 20% of pay (excluding local pay) i.e. total emoluments of Rs. 2307. Prior to his appointment, he was Currency Officer, Reserve Bank of India, New Delhi. He was also the Bank's nominee on the Board of the Corporation.

15. *Madras Industrial Investment Corporation Ltd. :* The Chief Executive of this Corporation is the Secretary and Shri S. Rajaratnam, M.A., A.I.I.B. (54 years) was appointed thereto on 1st September, 1949. He draws Rs. 1800 plus D.A. of Rs. 150 and car allowance of Rs. 150

p.m. Earlier, he was Secretary of the Madras State Co-operative Bank Ltd. He also served in the Indian Bank Ltd. for ten years.

Appendix III to Chapter VI

A

Particulars of dates of Constitution, Composition and Functions of Executive Committees of SFCs.

All SFCs have set up Executive Committees in terms of Section 18 of the SFCs Act, composed of the Managing Director as Chairman, two directors elected by nominated directors—one each from among directors nominated by the State Government and by Reserve Bank and IFC, and one director elected by the elected directors; in case of Joint Financial Corporation, one director each by participating States. Details of these Committees of the various SFCs are as follows:

Andhra Pradesh : The Executive Committee was set up on 25th July, 1961. It screens applications and makes recommendations to the Board, besides approving expenditure on purchase of dead stock, etc. upto certain limits. It also approves arrangements to pay commission or exchange charges to banks and agents of the Corporation.

Assam & Rajasthan : The committees were set up on 14th August, 1954 and 2nd March, 1955 respectively and can sanction loans upto Rs. 1 lakh.

Bihar, Maharashtra & Uttar Pradesh : The committees were set up on 9th November, 1959, 16th August, 1962 and 3rd January 1955 respectively, and can sanction loans upto Rs. 1 lakh. While the committee in Bihar can vary the terms of loans sanctioned and exercise various powers under its Staff, Expenditure and Gratuity Regulations, the committee in Maharashtra can deal with all matters within the competence of its Board except sanctioning loans of above Rs. 1 lakh. The committee in U.P. can also appoint staff to posts carrying scales not exceeding Rs. 500.

Gujarat, Madhya Pradesh and Punjab : The committees in these Corporations were formed on 1st May, 1961, 23rd July, 1955 and 23rd February, 1957 respectively. They can sanction loans of upto Rs. 2 lakhs. The committees in Gujarat and Punjab recommend loan applications to the Board for amounts above Rs. 2 lakhs, while the latter can further reject any loan proposals irrespective of the amount. In Madhya Pradesh, the committee can deal with all matters within the competence of its Board except grant of loans of over Rs. 2 lakhs.

Orissa & West Bengal : The committees were set up in January, 1959 and May, 1954 respectively and can scrutinise all loan proposals and make recommendations to the Board and sanction expenditure under their Expenditure Regulations. In addition, in West Bengal, the Committee examines proposals for subscribing to debentures, guaranteeing

loans and deferred payments and underwriting of shares, etc. with powers to recommend to the Board for sanction or rejection (including loans).

Kerala : The committee was set up in 1953. It makes preliminary examination of applications for loans from the Corporation's funds and arranges for technical investigation and valuation of assets. It can dispose of applications under Agency Arrangements with State Government, for which purpose two representatives of Government also participate. Further, it attends to matters relating to appointment of staff upto the rank of officers.

Mysore : The committee was formed in April, 1959. It sanctions loans upto Rs. 1 lakh and recommends sanction/rejection in other cases. It also sanctions remuneration to Technical Advisers, recurring expenditure (except for creation of officers' posts) and non-recurring expenditure upto Rs. 15,000. It can appoint advisory committees for reporting on prospects of industries and evaluation of assets.

Jammu & Kashmir : The Committee was set up in January, 1960 (reconstituted in February, 1961) and considers loan applications and makes recommendations to the Board, and approves security documents. It can approve expenditure incurred by the Managing Director exceeding Rs. 500 in a month and purchase dead stock/other items as per the Corporation's Expenditure Rules.

Madras : MIIC has no such Committee ; the relevant provisions of SFCs Act do not apply to it.

B

PARTICULARS OF DATES OF CONSTITUTION, COMPOSITION AND FUNCTIONS OF ADVISORY COMMITTEES SET UP UNDER SECTION 21 OF SFCs ACT

Advisory Committees have been set up by only five SFCs, viz., Assam, Kerala, Madhya Pradesh, Punjab and West Bengal. MIIC has no Advisory Committee, as the relevant provisions of SFCs Act are not applicable to it ; special committees are formed by it for considering applications for underwriting and equity participation.

Maharashtra SFC has no standing committee. It appoints such Committees for technical and other advice, consisting of its directors and officers or other persons as determined by its Board. Details of the committees of the five SFCs referred to above are as follows:

(1) *Assam* : This Corporation has a Tea Advisory Committee set up on 26th March, 1955, and a Tripura Advisory Committee set up on 21st January, 1961. The former includes four directors of the SFC and eight other persons actively associated with the tea industry in Assam. It gives advice on the general policy regarding sanction of loans to tea gardens including technical advice. It also conducts inspections/valuation. The latter committee consists of experts from tea industry and persons having intimate knowledge of the scope and prospects of indus-

tries in Tripura and advises in the matter of sanctioning loans to concerns situated in Tripura.

(2) *Kerala :* Regional committees have so far been set up in five out of nine revenue districts, viz., Trichur, Kottayam, Quilon, Trivandrum and Malabar ; each committee consists of the Corporation's Chairman, the Managing Director and the director with headquarters within the concerned district. The Corporation also utilises the services of non-official experts and institutions. These Committees give detailed information regarding the Corporation's functions and procedure for applying for and getting assistance from it.

(3) *Madhya Pradesh :* The Corporation set up its Advisory Committee on 3rd October, 1961 consisting of the Managing Director as Chairman and eight industrialists, engineers, etc. It gives technical and other advice.

(4) *Punjab :* The Corporation has at present Advisory Committees for the following industries, viz., (*i*) General engineering, (*ii*) Textiles, including hosiery, (*iii*) Cold storage and (*iv*) Electric supply undertakings, consisting of three directors, including the Managing Director as Chairman and two members from each of the industries except the General engineering industry, which is represented by three members. The Corporation also has panels for the Transport and Hotel industries. The President of the Federation of Hotel and Restaurant Associations of India is a member of the panel for the Hotel industry. Besides, an officer from the State Department of Transport/Tourism is invited to serve on these panels. These committees examine applications referred to them for technical advice and/or opinion about the scope of industries and extent of financial requirements of applicants before submitting applications to the Executive Committee/Board for decision.

(5) *West Bengal :* An Advisory Committee was set up on 22nd March, 1962, consisting of the Managing Director as Chairman and four members of the public actively associated with industries in North Bengal. Being largely experimental, the Committee has not yet been allotted specific functions.

Chapter VII

SUMMARY OF RECOMMENDATIONS AND SUGGESTIONS

Recommendation/Suggestion together with Chapter and paragraph references

Genesis & present structure of term lending institutions

The activities of the various institutions providing term finance to industry in the private sector may be duly co-ordinated to avoid overlapping of operations and to enable joint provision of loans and underwriting facilities, wherever necessary. There is also need for co-ordination between SFCs and IFC on the one hand and ICICI on the other. (II-29)

NSIC may concentrate only on promotional activities and give up its machinery hire-purchase business, which SFCs should take up. All small industrialists wanting machines on hire-purchase basis should only approach SFCs for their requirements, NSIC acting as a clearing house for information regarding availability, price, performance, etc. of different types of machines, and also as agent of SFCs for procurement of machines, wherever required. Regarding uneconomic applications involving small amounts, either Government may give a direct subsidy to SFCs on a suitable formula, or SSICs may handle such applications. Before SFCs can take up this business, the Act will need to be amended. After this, in one or two selected States, all hire-purchase applications may be dealt with by SFCs, with NSIC acting as clearing house for information. Senior officers of NSIC may be associated with the management of these SFCs in the transitional phase. (II-35/36)

It is desirable to arrange to meet a part of the foreign exchange needs of SFCs to enable them to finance more industries requiring imported machinery. If this is done, ICICI and IFC may informally undertake that normally they would not entertain applications for foreign exchange loans below an agreed figure, to avoid duplication of facilities which SFCs could provide. (II-37/38)

Further proliferation of institutions with similar functions and jurisdictions may be avoided. There is need to prevent duplication of SFCs' functions by SSICs/SIDCs and to bring about co-ordination in activities. SSICs may provide marketing facilities for small industries' products, supply of raw materials, etc. Supply of machinery on hire-purchase basis should be taken up by SFCs; applications for very small amounts may go to SSICs which should not normally grant direct loans and advances. (II-39)

The operations of SIDCs may be restricted to promotional functions e.g., formulating, executing and running of industrial projects. SIDCs should assume risks which SFCs do not normally undertake, and

should not make direct loans and advances to industrial units, at least within statutory limits permitted to SFCs. Funds proposed to be advanced by State Governments to industrial concerns on a commercial basis may be routed through SFCs. (II-40)

Resources of SFCs—Their sources of supply and cost

If SFCs are to seriously develop their business, particularly underwriting, and gradually also equity financing, then such Corporations which undertake these businesses on a sufficiently large scale would need to have a stronger capital base to absorb shocks of likely losses. (III-7)

SFCs (other than those of Kerala and Maharashtra) and the concerned State Governments may expedite completion of the preliminaries for accepting deposits. States may straightaway extend guarantee for deposits upto the ceiling permitted in the SFCs Act. (III-10)

As SFCs cannot provide depositors with the facility of advances against their deposits, they may, where necessary, offer upto 25 nP. per cent per annum more interest than medium-sized commercial banks. (III-12)

SFCs may fix such minima for individual deposits as would enable them to take full advantage of raising resources by deposits. (III-13)

The rates of interest offered by MIIC are rather high and should be brought into closer relationship with the general structure of rates for term deposits. (III-13)

With adequate publicity, canvassing and local patronage, SFCs may be able to attract reasonable amounts of deposits including those of trust funds. Local Bodies like municipalities, etc. may be persuaded to deposit their surplus funds with SFCs. SFCs may consider joining together to undertake an intensive all-India campaign to advertise the various facilities they offer to the public. (III-14)

Deposit receipts issued by SFCs may be made assignable to third parties. Such assignment may be exempted from stamp duty and State Governments may take necessary action in this behalf. (III-15)

SFCs may be permitted to receive deposits upto twice their paid-up capital. (III-16)

The borrowing limit under Section 7(5) of the SFCs Act may be relaxed from 10 times the paid-up capital and reserve fund to 15 times. (III-20)

SFCs may enter into an arrangement with LIC by which it would be prepared to invest, on demand, upto 2% to 3% of its total investments in their bonds. SFCs could then draw funds according to, rather than in anticipation of, their requirements. (III-26)

State Bank may extend more support to SFCs' bonds in future. Attempts should also be made to interest other institutional investors and individuals in these bonds. (III-27)

States may examine if they can include the probable requirements of the Corporations while drawing up their own annual loan

programmes, and transfer such funds to them on the same terms on which these are borrowed, sharing the expenses of floatation on a pro-rata basis. (III-30)

SFC bonds may be more attractive to institutional and other investors if their maturity-pattern is biased in favour of shorter periods; SFCs can float bonds of different maturities, the shorter maturity bonds for banks and individuals and the longer ones for institutions like LIC, trusts, etc. (III-32)

The statutory limit for borrowings from Reserve Bank for periods of 18 months may be increased from 60% of the paid-up capital of a SFC to 100%. (III-37)

As matters stand, SFCs cannot get reimbursement finance from Reserve Bank under Section 17(2)(bb) of the Reserve Bank of India Act. This provision may, therefore, be deleted from that Act. (III-39)

Government may agree that some part of the large annual flow of resources to employees provident funds may be invested in SFCs' bonds. (III-46)

Government may recognise both the bonds and deposit receipts of SFCs as approved securities under Section 11(2)(b) of the Income Tax Act; investments in them by charitable institutions would then be exempted from income tax. (III-46)

Additional funds should be made available to SFCs either by Government, as in the case of IFC, or by Reserve Bank, the latter through a National Industrial Credit (Long Term Operations) Fund to be created on the lines of the National Agricultural Credit (Long Term Operations) Fund which had been established to assist co-operative financing institutions. (III-46)

Deployment of resources

To avoid capital depreciation and losses, SFCs should, as far as possible, invest in short-dated securities. (IV-4)

To broaden the existing and potential investor-participation in industry, SFCs should finance equities and debentures. SFCs Act should be amended to authorise SFCs to directly participate in the equity of corporate industrial units. SFCs should also devote more effort to develop debenture-financing. (IV-7/8)

In the initial stages, SFCs should invest in or underwrite debentures in participation with IFC/ICICI; they may also enter into participation arrangements with these and other experienced financial institutions in the matter of extension of loans and guarantees as they will considerably benefit from such association. (IV-9/V-57 & 59)

SFCs may make a beginning by financing equities of seasoned enterprises and those with which they have had satisfactory dealings as lenders for a fairly long time. They could later undertake equity financing in respect of new ventures. It may also be desirable to fix a ceiling, say

30% of capital and reserves, upto which each SFC may engage in the business of equity financing. (IV-10/12)

Lag in disbursements as compared with sanctions may be dealt with by SFCs by levying a commitment charge on undrawn balances. (IV-13)

SFCs having idle funds may, instead of investing these in Government securities and bank deposits at low interest rates, lend to other needy SFCs, at an interest rate at which the funds had been borrowed or a slightly higher rate. If necessary, the Act may be amended for the purpose. (IV-14)

The provision regarding taking "sufficient" security under Section 25(2) of the Act should be amended so that the SFCs in their lending operations may place greater emphasis on the prospects of the industrial concern than on the security available. (IV-67)

With a view to assisting deserving industrial units, SFCs might consider accepting second-hand machinery as security as also the market value of security offered by borrowers instead of book value (IV-43/46). Where title to land taken as security is not quite clear, State Governments may take suitable steps to remove the defects (IV-48). Pending completion of examination of legal title to land, buildings, etc. belonging to applicant industrial units, SFCs might also consider granting interim loans in suitable cases as is done by IFC (IV-31). Personal guarantees of directors of joint stock companies, with good past record, may also be waived (IV-43). In order that the borrowing units may not experience any difficulty in securing working capital from banks, the mortgage deeds obtained by SFCs may, as far as possible, provide that their charge over the liquid assets would rank after the charge of commercial/co-operative banks providing working capital loans to the units (IV-40). To minimise risks, SFCs may make greater use of the Credit Guarantee Scheme for small industries wherever possible. (IV-65)

SFCs should foster projects and guide would-be entrepreneurs in the preparation of suitable projects and steer different schemes until they fructify (IV-31/VI-50). A drive for mutual understanding and persuasive effort on the part of the Corporations, including guiding borrowers in keeping books of accounts in acceptable form, is also required (IV-56). All Corporations may adopt the application form for small units suggested by the Committee set up on the recommendation of the Hyderabad Seminar (IV-34). It will pay SFCs to concentrate their resources on units which have a higher growth-potential and profit-earning capacity (IV-62). More concern with earning prospects and less with security especially where projects are economically viable and borrowers satisfy the tests of technical competence and personal integrity will enable SFCs to help deserving and new enterprises by relaxing margin requirements. (IV-54/64)

Staff of SFCs handling loan proposals should be familiar with the essential requirements of appraisal of term credit (IV-51). For new units or in the initial period of a loan to an existing unit, borrowers should

be required to submit frequent reports. SFCs may also frequently inspect new and more risky enterprises (IV-59). Besides, SFCs should be equipped fully for post-credit services (IV-66). For these purposes, SFCs should have a minimum complement of one team of trained and experienced persons from each of the three fields—engineering, industrial economics and accounting, at a fairly senior level; till this is done, they may consider drawing up a list of engineers and accountants serving in different industries within their jurisdiction and willing to advise on technical problems on suitable payment. The possibility may also be examined of setting up an independent technical and economic evaluation institution, with branches in important centres, to serve the evaluation needs of SFCs and other lending agencies like IFC, ICICI and commercial banks. (IV-62/VI-45/51)

The present lending rates of SFCs require to be adjusted to allow them a margin of at least 2½%. (IV-74)

Instead of a standard interest rate on all loans, SFCs may try to evolve an appropriate rate structure, the rates varying with the risk-rating of propositions, their size, period, etc. (IV-75)

All State Governments may soon implement the recommendations of the Small Scale Industries Board regarding reduction of stamp duty and other charges levied on loans to small units. (IV-86)

As a rule, working capital should be obtained from commercial banks, and SFCs might provide the permanent or initial working capital included in the cost of the project. (V-40)

All SFCs may show loans disbursed under agency arrangements in their balance sheets, together with the amounts outstanding to State Governments on their account. (V-42)

To make it worthwhile for SFCs to undertake agency functions, their commission may be on the same basis as in Maharashtra i.e. on the basis of the amount outstanding plus an annual subsidy for administrative expenses. State Governments may pay the agency commission to SFCs promptly, as and when due. (V-44/45)

ICICI, which does not have any branches, may appoint SFCs as its agents for various functions, including periodically inspecting borrower-conerns on its behalf. (V-54)

Working Results—Fiscal concessions, Management, etc.

As long as their post-tax profits cannot meet total dividend liability, SFCs would continue to draw subventions. This situation can be met, inter alia, by Government exempting from tax 25% of SFCs' annual pre-tax profits which should be credited to the Special Reserve Account, till such credits add up to the paid-up capital. (VI-17/18)

The present ceiling of accumulations in the Special Reserve Fund, built out of dividends forgone by the States and Reserve Bank, viz. 10% of the paid-up capital of a SFC, is too low. It may be made at least 25% of the paid-up capital. (VI-20)

The existing subvention liability of SFCs may be written off. (VI-22)

State Governments may waive their right to appoint an auditor and be satisfied with audits (*i*) by the auditor appointed by shareholders other than the State Governments and Reserve Bank and (*ii*) by the Auditor General till such time as this is done statutorily under Section 37(6). When the latter audit ceases and any State Government has special reasons for wanting an audit in addition to the one conducted by the auditor appointed by the other shareholders, it may request the Auditor General to undertake an audit under Section 37(6). This will require the existing Section 37(1) to be amended. (VI-26)

Inspection of SFCs by Reserve Bank should be carried out at least biennially. Their scope may be enlarged to examine how far SFCs are performing the functions for which they were set up and those which are called for in the context of a policy of rapid industrialisation. (VI-29)

The Boards of SFCs may be enlarged to provide for a separate seat for financial institutions other than scheduled banks and LIC (VI-33).

Government may try to get the assistance of the Development Banks Services Department of the International Finance Corporation to give orientation courses in term lending to Managing Directors and senior staff of SFCs. (VI-34)

SFCs may appoint younger men as Managing Directors, who would serve longer tenures. It is not advisable to appoint Government officials to these posts, unless they are adequately qualified and can be left undisturbed for at least four years; otherwise, suitably qualified outsiders may be appointed as permanent employees of the Corporations. (VI-34 & 37)

The Boards of SFCs should delegate to their Executive Committees power of sanctioning loans upto Rs. 2 lakhs in each case. (VI-39)

SFCs may be associated with Governmental and other agencies which undertake research or surveys for uncovering fresh investment opportunities within their areas of operation. SFCs and the States may also consider the proposal of Rajasthan SFC for a "cell" to assist and guide intending industrialists. (VI-50)

To fulfil the expectations entertained of them, SFCs have to assume risks. Their management must combine good judgement and imagination, and strike a balance between excess caution and excess risk-taking. (VI-52)

Opening of branch offices of a SFC should be decided on merits. If business at any selected centre grows, the SFC may consider setting up a small branch there. Before doing this, agency arrangements may be entered into with branches of the State Bank at selected centres where small advisory committees may also be formed to advise SFCs. Commercial banks can also act as agents of SFCs where the latter have no branches. (VI-53/V-61)

Some SFCs hold Board meetings at different centres in the States. Others may adopt this practice. (VI-53)

Each SFC should have a small statistical cell. As its operations grow, it will need to maintain detailed statistics to assess the progress of the borrowing institution and also find out where gaps lie. (VI-54)

The minimum set of books of accounts recommended by the Sub-Committee of the Committee on Credit Facilities of the Small Scale Industries Board for adoption by small scale industries may be tried out by Government on a 'pilot' basis in selected areas, and then prescribed for adoption. Government may, in due course, make it obligatory for units seeking assistance either from Government under the State Aid to Industries Act, or from SFCs or NSIC, to maintain certain minimum accounts on standardised patterns, and submit such information as may be required to process their applications and assess the progress made by them from time to time. (VI-55)

WORKING GROUP ON STATE FINANCIAL CORPORATIONS

QUESTIONNAIRE I FOR STATE FINANCIAL CORPORATIONS

1. (*a*) Please furnish the following figures in respect of the loan operations of your Corporation during 1959-60, 1960-61 and 1961-62 separately.

(*i*) Applications received during the year
No.
Amount

(*ii*) Applications sanctioned during the year
No.
Amount

(*iii*) Applications withdrawn during the year
No.
Amount

(*iv*) Applications rejected during the year
No.
Amount

(*v*) Applications pending at the year-end
No.
Amount

(*vi*) Total amount sanctioned at the end of each year (cumulative)

(*vii*) Total amount disbursed at the end of the year (cumulative)

(*viii*) Loans sanctioned but not to be made available
No.
Amount

If there are large year-to-year variations in these figures, please give reasons therefor.

Please give the number and amount of loans sanctioned in 1960/61 and 1961/62 to (*i*) small scale and (*ii*) other units (separately) in which the amounts applied for were reduced. Please indicate some of the reasons therefor.

(*b*) Please furnish the breakdown of applications rejected during 1961/62 according to the following categories:

(*i*) Inadequacy of security
(*ii*) Unsatisfactory title to security
(*iii*) Difficulties in having satisfactory title to security because of operation of Rent Act, etc. in certain States.
(*iv*) The scheme not being feasible—technically—financially.
(*v*) Inadequacy of creditworthiness of the borrower.
(*vi*) Other reasons, if any (to be specified).

2. (*a*) Of the loans sanctioned in 1961/62, what have been the

maximum and minimum periods between receipt of application and sanction of loans, separately for (*i*) small and (*ii*) other units?

(*b*) What are the usual factors responsible for the delay in sanctioning loans to (*i*) small scale and (*ii*) other units?

3. (*a*) Of the loans disbursed in 1961/62, what have been the maximum and minimum periods between the sanction of loans and their disbursement, separately for (*i*) small and (*ii*) other units?

(*b*) What are the usual factors responsible for delay in disbursements of sanctioned loans to (*i*) small scale and (*ii*) other units?

4. Section 25(2) of the State Financial Corporations Act requires their advances to be "sufficiently secured". This is generally being taken as the basis for insisting on a margin of 50% in the value of the security. Recently some State Financial Corporations have relaxed margins in certain cases. But this rigid adherence to margin rules out the emphasis on the character and antecedents of the borrower, his past performance, and the prospects of the industry as well as of the particular unit under scrutiny. If adequate attention is to be paid to these latter criteria, will that create any practical difficulty in varying the margin on the basis of such criteria? Thus e.g., if in your opinion, the earning prospects of the unit, and your assessment of borrower are (*i*) extremely good, or (*ii*) good or (*iii*) not so good, would it be possible for you to relate your margin to the type of prospects envisaged?

5. Do the State Financial Corporations encounter competition from other credit institutions like commercial and co-operative banks, Industrial Development Corporations and Small Industries Corporations, etc. in the extension of loans to industrial concerns? If so, what steps would you suggest to regulate such competition?

6. Section 25 of the State Financial Corporations Act permits the Corporations to underwrite the issues of shares, debentures, etc. of industrial concerns, and give guarantee for deferred payments in respect of purchase of equipment from indigenous sources. What are your detailed suggestions including the limits and safeguards necessary to undertake this operation?

7. (*a*) During 1960/61 and 1961/62, what proportion of your sanctions related to small units?

(*b*) What steps can be taken to provide more assistance to such units?

(*c*) What are the number and amount of your loans to small units now outstanding which are guaranteed under the Guarantee Scheme of the Government of India?

(*d*) Is this scheme useful to the Corporations?

(*e*) If not, what are your suggestions to make it so?

8. How can State Financial Corporations be made to play a more active role in financing industrial co-operative units?

9. What are the existing facilities for technical consultation and scrutiny of industrial projects? How far are these adequate and can be improved and enlarged, and from what source?

10. (*a*) What are the existing arrangements for publicising the activities of State Financial Corporations (through brochures and pamphlets in local languages, advertisements in newspapers, magazines, etc.) and how far have they been useful? What further steps can be taken in this direction?

(*b*) What is the existing machinery for public relations to explain to prospective borrowers the facilities which State Financial Corporations offer and their terms? If this is wanting, what are your suggestions?

(*c*) Have State Financial Corporations made use of chambers of commerce or other industrial associations or publicity organisations of the State Governments to make their functions known to as many industrialists as possible?

(*d*) Has any special promotional activity been undertaken in your State, such as a survey of industrial units or potential in specific areas, and has any other direct approach been made to the borrowers? Have you any suggestions in this regard?

11. Do you think the business of State Financial Corporations can be expanded—either by getting deposits or by making more loans—through the establishment of branches? Alternatively, would you suggest any agency arrangements with banks? Have you any experience either with branches or agency arrangements?

12. (*a*) What rates of interest are charged on loans sanctioned since 1960-61?

(*b*) Do the rates vary with the duration of the loan, security offered, etc.?

(*c*) If not, have you any suggestions in this regard?

(*d*) Do you feel that working capital loans should bear the same rate of interest as block loans?

13. In addition to the facilities which each State Government now extends to the State Financial Corporation, like contributing to its capital and relinquishing for some years the dividends on such shares to build up the Special Reserve Fund, guaranteeing (*a*) dividends on the entire paid-up capital of the Corporation, (*b*) deposits, (*c*) bonds and debentures and (*d*) advances from Reserve Bank against eligible bills, etc., are there any other special facilities which it can give to the Corporation to improve its usefulness?

14. (*a*) Has the Corporation adopted the simplified application form for small scale industries suggested by the Committee appointed by Reserve Bank in 1959 on the recommendation of the Hyderabad Seminar on the financing of scall scale industries? Please

enclose copies of the application forms now used for small scale and other units.

(*b*) Please describe briefly the procedure followed in processing a loan application from the time it is received till the first instalment of the loan is disbursed.

(*c*) What is the system of valuation of assets? Is this entrusted to public valuers or has the Corporation engaged a part or whole-time valuer? What are your suggestions for getting valuation done efficiently and expeditiously?

(*d*) What are the criteria for valuation of (*i*) land, (*ii*) buildings and (*iii*) plant and machinery? Are loans sanctioned before valuation and legal clearance of assets offered in security? What are the pros and cons of the practice actually followed?

(*e*) Is there any difficulty in your State regarding clarity of title to the land which is offered in security? If so, how can it be overcome?

15. Have there been any complaints that the procedure followed by the State Financial Corporation in sanctioning loans is rigid or time-consuming? How to remedy such complaints?

16. What are the prospects of State Financial Corporations making loans in participation with other credit institutions such as commercial banks, Industrial Finance Corporation of India and Industrial Credit and Investment Corporation of India Ltd.? What should be the general terms and conditions of such participation, including such matters as scrutiny of applications, security, servicing of the loans, etc.?

17. What are the terms governing loans to units situated in rented premises? Have the borrowers or SFCs experienced difficulties due to restrictions imposed by the Rent Act in the State, and has the State Government been moved in this matter?

18. (*a*) Generally speaking, is there a demand for working capital loans along with the block loans?

(*b*) Please give the following information regarding working capital loans sanctioned by you:

	1960-61		1961-62	
	Small units	Other units	Small units	Other units
(*i*) Total sanctions of loans which include working capital component				
No. of loans				
Amount				
(*ii*) Working capital component in (*i*) above				

(c) What is the basis for sanction of amounts for working capital? For units to which you make working capital loans, do you make an estimate of their minimum working capital requirements in the next 2/3 years? If so, do you prescribe that the working capital of the unit should never fall below this estimated minimum? If this procedure is not followed, how is it ensured that the loan for working capital is utilised only for this purpose?

(d) Do you know of instances where your borrowers have suffered from inadequate working capital? If so, why could they not be accommodated by (i) you and/or (ii) a bank?

(e) In what ways can your present practice regarding giving working capital loans be changed to give greater facility to borrowers?

19. (a) Have the SFCs been confronted with any special difficulties in raising the required funds?

(b) Is the raising of funds in the form of deposits more convenient or economical than by issue of bonds?

(c) What is your experience of floating bonds and debentures? Have you any suggestions regarding their size, rate of interest, period of maturity, time for floatation, etc.?

(d) Do you anticipate any difficulty in availing of the refinancing facilities from the Refinance Corporation for Industry Ltd. after this Corporation is notified by Central Government in terms of Sec. 7(4) of the SFCs Act as recently amended? If so, how can it be removed?

(e) How have the surplus resources of the SFC been invested so far and with what returns? Have you any suggestions in this regard?

20. Is the State Government channelling through the SFC its own loans to small units under the State Aid to Industries Act? If so, please give the amounts placed at the disposal of the SFC annually during 1959-60 to 1961-62 and the amounts actually disbursed by the SFC to borrowers in these years, and the terms governing such loans and the agreement between the SFC and Government. If not, please explain reasons therefor.

21. (a) Have any periodical returns been prescribed from borrowers to watch the utilisation of loans? If so, please enclose a set of these. Please indicate some of the major items for which follow-up data are obtained.

(b) Do borrowers supply the data asked for? If not, what difficulties do they encounter, and how can these be removed?

(c) Do you feel that your returns give you enough data to watch utilisation? If not, what are your suggestions for modifying them?

22. (*a*) Do you inspect units financed by you?

(*b*) Are all units inspected or selected ones?

(*c*) How often is that done?

(*d*) Have you prescribed any inspection forms? If so, please enclose a set.

(*e*) What is your inspection staff?

(*f*) How are corrective measures suggested by inspection enforced if terms of the loan have been wilfully or otherwise violated? Please give a few case studies of this.

23. (*a*) Please attach statement of the strength of senior officers and other staff (excluding clerks, typists, peons, etc.) of the Corporation and their pay scales, allowances, etc. Please send a copy of your Service Rules.

(*b*) Please give particulars of the Managing Directors of the Corporation (Secretaries in the case of the Madras Corporation) since inception.

(*c*) How many of the existing officers other than the Managing Director have training in banking or accountancy? Have you any suggestions regarding the strength, qualifications, remuneration, etc. of the officers?

(*d*) Please give particulars of nominees of the State Government, the Reserve Bank of India, and the Industrial Finance Corporation on the Board of the Corporation since inception.

24. Please indicate any other provisions in the statute of State Financial Corporations or their General Regulations, Rules, instructions issued by State Governments, etc. which inhibit the progress of these Corporations.

QUESTIONNAIRE II FOR CHAMBERS OF COMMERCE, INDIVIDUALS, ETC.

1. Have State Financial Corporations (SFCs) accomplished, by and large, the purpose for which they were set up? If not, what, in your opinion, are the impediments? What steps do you suggest to remove them?

2. Are there, in your opinion, any particular aspects of the working of the Corporations which hinder their progress? If so, what are they and what are your suggestions for improving them?

3. Are the procedures and practices of the Corporations dilatory or unduly costly and stand in the way of industries getting adequate

and timely assistance from them at reasonable cost? Have you any suggestions in this regard?

4. Do you consider the lending criteria of the Corporations (e.g., in regard to nature and extent of security demanded, margin, etc.) onerous? What relaxations do you suggest consistent with the safety of the Corporations' funds?

5. Are there any other difficulties which prevent the industrial concerns—both small and medium-sized units—from availing themselves of assistance from SFCs and what steps should be taken by the Corporations to provide more assistance to such units?

6. To what extent would the usefulness of the Corporations be increased by the recent amendment of the SFCs Act in terms of which the upper limit of loans to industries organised as public limited companies and industrial co-operatives has been raised from Rs. 10 lakhs to Rs. 20 lakhs?

7. Would the borrowing units find it more convenient to obtain both equipment loans and working capital loans from the SFCs instead of securing the latter from banks? If so, please furnish reasons and indicate the nature of arrangement which would be convenient for providing working capital loans.

8. What are your views regarding grant of loans for relatively large projects by SFCs in participation with other credit institutions, viz., banks, Industrial Finance Corporation, Industrial Credit and Investment Corporation of India Ltd.? Please suggest the lines on which such joint lending could be arranged.

9. What are your views regarding the Corporations engaging in underwriting issues of shares and debentures of *medium and small-sized industrial concerns,* and giving guarantees for deferred payments in respect of purchase of equipment from indigenous sources?

10. Do you consider that any special facilities should be given by State Governments to the Corporations in order to improve their usefulness?

11. What assistance can your Chamber/Association provide to the SFCs (*a*) for technical consultation and scrutiny of industrial projects and (*b*) in other respects?

12. Please give details regarding complaints, if any, received from your members in the matter of obtaining financial assistance, etc. from SFCs.

13. Do you think the Corporations would be able to serve the industries better without increasing the cost of credit to any large

extent if they establish one or more branch offices at important centres in the State?

14. (*a*) Are the existing arrangements for publicising the activities of the SFC in your State (through brochures and pamphlets in local languages, advertisements in newspapers, magazines, etc.) adequate? What further steps do you suggest in this direction?

(*b*) In what ways do you think SFCs can make use of the good offices of Chambers of Commerce or other industrial associations to make their functions known to as large a number of industrialists as possible?

15. Please give any other suggestions you may have to increase the scope of SFCs' activities and make them more effective instruments for term finance to small and medium-sized industrial units.

Questionnaire III For Foreign Development Banks

(Please mention the date for which figures are given..................................)

A. Constitution and Management

1. When did your bank commence business? Was it established under (*a*) statute or (*b*) the general corporation laws of the country?

2. Is your bank (*a*) State-owned, or (*b*) privately-owned, or (*c*) a mixed venture?

3. What is the size and constitution of the Board of Directors? Please indicate the interest represented, the selecting and appointing authorities, period of appointment, etc. for directors.

4. (*a*) Do you employ any special technical staff for appraisal of loan applications? Are they employed on full or part-time basis? Are there arrangements for sharing technical staff with other organisations?

(*b*) What type of credit or economic intelligence unit do you have?

(*c*) Do you employ the services of consultants?

5. What is your relationship with (*a*) the Government and (*b*) the the Central Bank of your country, in broad policy matters?

B. Resources

6. (*a*) What are the (*i*) authorised, (*ii*) subscribed, and (*iii*) paid-up capital of your bank?

(*b*) Please give details of the present ownership of equity capital—

	Amount	Percentage
(*i*) Government		
(*a*) Central		
(*b*) State		
(*c*) Local		
(*ii*) The Central Bank		
(*iii*) Commercial banks		
(*iv*) Other institutions (please specify)		
(*v*) Individuals		
(*vi*) Foreign participation		
(*a*) Institutions (please specify)		
(*b*) Individuals		
Total		

7. What is the maximum upto which you can borrow from various sources? Are there also limits to borrowings from individual sources?

8. (*a*) Can you float bonds and debentures? If so, under what conditions? Does the Government guarantee repayment of principal and payment of interest on these bonds, etc.?

(*b*) Please give details of the present ownership of your bonds and debentures—

(Date.......................)

	Bonds	Debentures
(*i*) Government		
(*a*) Central		
(*b*) State		
(*c*) Local		
(*ii*) The Central Bank		
(*iii*) Commercial banks		
(*iv*) Other institutions (please specify)		

(*v*) Individuals
(*vi*) Foreign participation
(*a*) Institutions
(please specify)
(*b*) Individuals

Total outstanding

9. (*a*) Has your bank received financial assistance from any foreign government or institution, including IBRD? Please give details:

Source	Whether loan or grant	Date	Amount	Period of loan	Purpose (if specified)	Whether repayable in local currency or foreign exchange	Remarks

(*b*) What has been the practice with respect to the foreign exchange risk on external loans?

10. (*a*) In addition to the above, can your bank borrow from any other internal source, such as the Government and the Central Bank? If so, under what conditions (period, rate of interest) and on what security can it borrow?

(*b*) Please give the total amount now outstanding.

11. Is any restriction placed on the type of security against which the bank may borrow?

12. Do you accept deposits from the public? If so, please indicate period(s), rate of interest, and conditions for withdrawal.
How do these conditions, especially the rates of interest paid by you, compare with those offered by other borrowers in the money market? What is the amount of such deposits currently outstanding? What are the main categories of depositors (individuals, private institutions, business concerns, etc.)?

13. Is there any arrangement by which your Government places certain funds at your disposal to be re-lent to certain preferred sectors (e.g., small industries, export industries, etc.)? Please give details regarding amounts so received in the last 2/3 years, rates of interest payable and chargeable by you, and other conditions.

14. Have you any facilities to get refinance for some of your loans and advances?
What are the terms and conditions? How far have you used them and found them adequate?

C. Investment

15. (*a*) What conditions are laid down in your Charter to govern the investment of surplus funds?

(*b*) Are you prohibited from making certain specific types of investments? Must certain sums be invested in Government or any other approved securities? Are limits, upper and lower, fixed for any individual investments?

16. Please give total of your present investments.

D. Loans and Advances

17. What regulations, in terms of your Charter, govern your loan policy?

(*a*) Is there any maximum or minimum limit placed on the size of any loan?

(*b*) Are all industrial units eligible for loans? Or are there any restrictions e.g., on the size of capital structure, employment, types of industry, purpose for which loan is sought, etc.?

(*c*) Are there any restrictions on the term of loan? What is the average, maximum and minimum term for which loans are given?

18. Please give details of the loan operations of your bank in the last two years.

Year	Applications received		Applications sanctioned		Amount disbursed
	No.	Amount	No.	Amount	

19. How many applications were rejected in the last two years? What are the principal reasons?

20. What is the average time-lag, say, in the last two years, between (*a*) the receipt of loan application and granting of the loan and (*b*) the granting of the loan and its disbursement? What are the principal reasons for these two kinds of time-lag?

21. In sanctioning loans do you give preference to particular industries? If so, why? Please also indicate if, in your loans and advances policy, the bank is expected by Government to follow any particular pattern—say, assisting certain special groups of industries, etc.—in conformity with the policy of industrialisation adopted by your country. Do you get any such advice from Government from time to time?

22. What is the proportion of loans and investments which have so far been made to (*i*) new enterprises and (*ii*) existing enterprises to total loans?

23. (*a*) Please give, if possible, an industry-wise breakdown of the loans currently outstanding (or total of loans granted).

Industry	No. of loans	Amount

(*b*) Please classify also your present loans according to the size of loans sanctioned—classified into 4/5 slabs of size as per proforma below:

Size of loans sanctioned	No.	Amount

24. What broad criteria must an applicant-unit satisfy for obtaining a loan? Please enclose an application form. If a unit is not able to supply the full data, what other steps would you take?

25. Please describe briefly the method of appraisal of applications. Have you prescribed any written instructions for the guidance of your appraisal staff? If so, please enclose a copy.

26. Is the borrowing unit inspected either before the grant of a loan or after? Please enclose a copy of any inspection report form.

27. (*a*) Do you undertake any loan supervision or follow-up surveys? Please give details and enclose a copy of form which may have been prescribed for this purpose.

(*b*) Does the borrowing unit furnish any periodical returns? If so, please give forms prescribed for this.

(*c*) Do you always appoint a director on the Board of the borrowing concern? If so, what is your experience?

28. (*a*) What securities do you accept for loans? What is the usual margin maintained? Are there any statutory provisions relating to security?

(*b*) Do you give loans on the guarantee of third parties, like the Government? If so, are security requirements relaxed for such loans?

29. In drawing up loan agreements, does your bank introduce any restrictive covenants? What types of such covenants are generally introduced?

30. Is repayment schedule uniform for all loans, or does it vary with each loan?

31. What is the interest policy of your bank? Is the same rate charged on all loans or does it vary? If the latter, what considerations determine it? What are the maximum, minimum and average rates charged during last two years?

32. Do the functions of your bank include the underwriting of shares? To what extent have you undertaken this activity? Please give details, including the terms and conditions. Is there any need for further developing this function? Does it require any modification of your present procedure?

33. What is the total value of equity capital subscribed by the bank since 1955? (Please specify).

34. Do you stand guarantee for your borrowers' commitments to third parties? Please give details.

35. What, according to your experience, is the minimum economic size of a loan the income from which can cover your costs of administration and prior study, etc?

36. How far and in what manner has your bank helped in securing foreign collaboration for your borrowers? Please give details.

Do you enjoy any special tax-concessions or privileges as a development institution? Are these temporary or in perpetuity? Please give full details.

38. Have you given any loans in participation with other institutions like banks—domestic or foreign? If so, please give total of such loans in last three years, and the terms of your participation.

39. What in your view, has been the role of your bank in the recent economic development of your country? Have you undertaken any special promotional campaigns to acquaint banks and potential borrowers with your services? How far do you think they have borne fruit?

40. Have you, in recent years, undertaken a comprehensive assessment of the working of your bank? As a result, are any measures contemplated to expand the scope and size of your operations, by strengthening your human and material resources, covering new sectors of the economy, etc.? What are your suggestions to this end?

41. Are there also other institutions in your country offering term finance to industry? In what manner are their functions co-ordinated with yours?

E. Profit Utilisation and Dividend Policy

42. Please give the profit and loss position of your bank since its inception.

Year	Profit earned	Loss sustained	Remarks

43. Does your Charter or any Government ruling limit, or prescribe the disposal of, your profits?

44. Please give details, with the amounts outstanding, of any funds created out of profits.

45. (*a*) Do you guarantee a minimum rate of dividend on your shares?
(*b*) Has it been paid out of profits or out of a special loan from Government?

46. Please give particulars of dividends declared since the inception of the bank

Year	Rate of dividend	Amount paid	Source	Remarks

Does the Government or other major shareholder(s) forgo, under certain conditions, the dividend and permit its transfer to a special reserve fund?

FOREWORD

The Industrial Policy Resolution, 1948, marked, as it were, the beginning of an era in the economic development of free India. It signified the adoption by Government of a positive policy of rapid industrialisation. Almost simultaneously, Government set up the Industrial Finance Corporation of India to assist industrial concerns by providing term finance and other measures of financial assistance. The operations of this institution were, however, statutorily confined to public limited companies and industrial co-operatives, and were likely to extend more to the comparatively large scale enterprises, and to leave out of their scope the wide field covered by proprietary and partnership undertakings which are also relatively small scale. The need was, therefore, felt for similar term lending institutions at the State level to finance the considerable sector of industry comprising the medium-small and small scale industrial units. Accordingly, legislation was promoted by the Government of India after considering the views of State Governments, and the State Financial Corporations Act, 1951, came into force on the 1st August, 1952. At present, there are fourteen Corporations set up in terms of this Act in all the major States except Madras where the Madras Industrial Investment Corporation incorporated under the Companies Act has been functioning since 1949.

While assistance provided to industry by State Financial Corporations appears to be gaining some momentum in the last few years, their performance generally has been below expectations, considering the size of investment in the private industrial sector contemplated under the Plans. In view of this, it was recommended by the Eighth Annual Conference of representatives of State Financial Corporations in November, 1961 that the Reserve Bank might set up a Working Group to review the working of State Financial Corporations, and suggest ways and means of improving their usefulness for accelerating the development of industries. The Working Group met, after some informal preparatory work in the Bank bearing on its scope of inquiry, for the first time in June, 1962. The Draft Report of the Group was placed for informal discussion before the Tenth Annual Conference in Bangalore in January, 1964 after which the final Report was submitted to the Reserve Bank of India on February 6, 1964.

The Bank wishes to take this opportunity to express its gratitude to the institutions which consented to make the services of their members available to the Working Group. The Bank also desires to record its appreciation of the co-operation extended to it by State Financial Corporations and development banks abroad by answering the detailed questionnaires issued by the Group. To the members of the Group the Bank owes its thanks for their labours in the preparation of this

comprehensive and valuable study. The views expressed in the Report are those of the members of the Working Group in their personal capacity, and do not commit in any manner the institutions which they represent.

Reserve Bank of India.
Central Office, Bombay.

B. K. MADAN
Deputy Governor

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NOTE: *In this Report, amounts are expressed in units of thousands, lakhs or crores of Indian Rupees. A lakh stands for one hundred thousand (1,00,000); a crore stands for a hundred lakhs (1,00,00,000). One Indian Rupee = 1sh. 6d. or Rs. 13⅓ = £1 Sterling and Rs. 4.762 = \$1 U.S.A.*